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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-777

IN THE MATTER OF

ROBERT E. CLEVELAND and FRANCES H. CLEVELAND, ON BEHALF OF THEMSELVES AND ALL OTHER TELEPHONE SUBSCRIBERS AND CUSTOMERS OF ILLINOIS BELL TELEPHONE CORPORATION SIMILARLY SITUATED,

Petitioners,

VS.

ILLINOIS BELL TELEPHONE COMPANY, an Illinois Corporation, and UNITED STATES OF AMERICA,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioners, Robert E. Cleveland and Frances H. Cleveland, on behalf of themselves and all other telephone subscribers and customers of Illinois Bell Telephone Corporation similarly situated respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals, Seventh Circuit, in the above cause.

(a)

OPINIONS.

The opinion of the United States Court of Appeals, Seventh Circuit is not reported in the Advance Sheets to date.

Two opinions of the United States District Court are reported in 319 F. Supp. 418 (October 16, 1970) and 325 F. Supp. 487, (December 11, 1970).

Two opinions of the United States District Court, the first denying the motion to remand the case to the State Court, and the second, dismissing petitioners' suit.

All of the foregoing opinions are set out in the Appendix at the end of this Petition for Certiorari.

(b)

JURISDICTION.

The jurisdiction of this court is invoked pursuant to Rule 23 on the following grounds:

(i) The judgment and opinion of the United States Court of Appeals was handed down September 22, 1971.

(ii) Not applicable.

(iii) Section 4254, Title 26, Internal Revenue Code, USCA, is being violated and nullified by respondent, Illinois Bell Telephone Company (hereinafter referred to as "Bell"), who is overcharging all telephone subscribers in

the Chicago area by charging "a tax on a tax." Namely, in calculating the 10% Federal excise tax on telephone calls, respondent charges 10% on both State of Illinois and City of Chicago taxes levied against telephone calls. It is this overcharge of a "tax on a tax" that petitioners contend is illegal, unlawful, and is merely an unwarranted and arbitrary overcharge by Bell. Petitioners contend that this is a controversy between Bell and the petitioners and all other customers in the Chicago area similarly situated. Further, petitioners contend that a representative or class action is proper and necessary in this cause to prevent a multiplicity of suits.

(c)
QUESTIONS PRESENTED FOR REVIEW.

(1) Did the United States District Court and Court of Appeals err in refusing to remand this cause to the State Court where the original suit was filed?

(2) Since the controversy was solely between Bell and its subscribers, was the United States a necessary party?

(3) Is this suit filed on behalf of all subscribers of Bell a representative suit or class action suit, or must each subscriber file a separate claim for refund from Bell?

(4) Is the overcharge by Bell of charging 10% on the State and City taxes on phone calls "a tax on tax" or is it a "service charge" as Bell contends?

These are the issues before this Court.

(d)

The only statute involved insofar as a statute forms the basis for Bell's overcharges of "a tax on a tax" is Section 4254, Title 26, USCA.

(e)

STATEMENT OF THE CASE.

This is a very simple case despite the complex decision of the United States Court of Appeals.

The petitioners filed a representative suit on behalf of themselves and all other subscribers and customers of Bell against Bell for Declaratory Judgment in the State Court of Cook County, Illinois, for a refund of overcharges by Bell.

The basic allegations in the Complaint are that Bell, without authority of law, was overcharging their subscribers and customers for a period of at least five (5) years prior thereto by collecting "a tax on a tax." The Complaint alleges that Bell was charging a 10% tax on the City and State taxes levied on all telephone bills.

Bell filed a petition in the State Court to remove the case from the United States District Court on the ground that federal taxes were involved. The case was duly removed to the United States District Court. Petitioners then filed their motion to remand the cause to the State Court on the ground that the Complaint was for wrongful overcharge and there was no question of a refund from the United States of America involved and that federal taxes were not involved. The motion to remand stated that the suit was "for wrongful overcharge by the defendant and it has nothing to do with a refund of taxes from the United States. The United States of America is not a party to this suit. The United States of America has no interest in said suit. No relief is sought against the United States of America. The only relief sought is against Bell, an Illinois Corporation, for wrongful charges made by it. The District Court denied the motion to

remand in a Memorandum Opinion, a copy of which is attached to this Petition.

Thereafter, petitioner, pursuant to leave of court, filed an Amended and Supplemental Complaint, seeking the same relief prayed for in the original Complaint, and adding United States of America as a party defendant.

Bell filed its Answer stating that federal taxes were involved; that no claim for refund had been filed; that such a filing for a refund with Internal Revenue Service was a prerequisite to maintaining any suit for refund and that the suit should be dismissed.

United States of America filed a motion to dismiss the Amended and Supplemental Complaint on the ground that the court lacked jurisdiction of the subject matter.

Petitioners filed a motion to deny the motion of the United States of America to dismiss the Amended and Supplemental Complaint.

A suit had also been filed in the United States District Court entitled, "Agron vs. Illinois Bell Telephone" seeking somewhat the same relief sought by petitioners but on a different theory.

The United States District Court in two Memorandum Opinions in the *Agron* case hereinbefore referred to found that the overcharge made by Bell was a "tax upon a tax", was improper, illegal and contrary to the statute but that each individual taxpayer had to file a separate claim for refund with Internal Revenue Service. These Memorandum Opinions are attached to his petition in the Appendix.

After arguments of counsel and the filing of a brief, the United States District Court entered its order on

December 18, 1970 dismissing Petitioners' Amended and Supplemental Complaint.

Petitioners appealed to the United States Court of Appeals and this case and the *Agron* case were consolidated for oral argument by said court.

Thereafter, on September 22, 1971, the United States Court of Appeals handed its opinion in the consolidated action affirming the decision of the District Court and further finding that the petitioners had no cause of action and entitled to no relief. Since there is only one opinion for this case and for the *Agron* case, this opinion is set forth in full in the Appendix attached to this petition for a writ of certiorari.

This petition for a writ of certiorari should be granted because it reveals that both the District Court and the United States Court of Appeals have erroneously held that petitioners' suit is a suit for a refund of taxes from the United States of America, when in truth and in fact, it is merely a suit for a refund from Bell for overcharges wrongfully made.

(f)

Not applicable to Judgment of Federal Court.

(g)

This court has jurisdiction where a suit filed in a State Court is erroneously transferred to the United States District Court and where the lower court has refused to remand the case to the State Court. Further, even if there is a question of federal taxes involved, the United States Court of Appeals committed plain error in holding that a claim for a refund must be filed with the Internal Revenue Service and in holding that this suit is not a representative suit or class action, but that each telephone subscriber must file a separate claim for refund.

(h)

REASONS WHY THE WRIT FOR CERTIORARI SHOULD BE ALLOWED.

1. The United States Court of Appeals in the above cause has misapprehended the issue by declaring that federal taxes are involved. This suit is a controversy between petitioners and those subscribers similarly situated and Bell. Petitioners have no quarrel with ~~United~~ States of America. United States of America submit no bills. United States of America collects nothing from petitioners. United States of America is not overcharging anyone. The Federal Statute, Title 26, Section 4254, does not sanction any overcharge. No relief has ever been sought from United States of America in petitioners' suit. All of petitioners' dealings are with Bell. Petitioners paid this overcharge to Bell. No one knows what Bell does with this money. Nowhere in any Federal statute are "charges for services" equated with State or local taxes. Bell merely has arbitrarily overcharged petitioners by adding on to the bill a 10% tax on State and City taxes.

2. "A tax on a tax" is illegal. The federal 10% tax on all local and long distance telephone calls imposed on the city and state taxes on such calls is clearly a tax on a tax and is contrary to the Federal Statute and contrary to common sense. (Title 26, Section 4254, USCA)

3. The United States District Court erred in refusing to remand the case to the State Court for disposition because all that is involved is the propriety of an overcharge by Bell.

4. Both the United States District Court and the United States Court of Appeals erred in holding that this suit was not a class action. To make each telephone subscriber file a separate claim for refund on the relatively small amounts involved is absurd, unfair, and so costly as to deprive the individual subscriber, as a practical matter, of his right to relief. (Title 28, Rule 23, Rules of Civil Procedure, USCA.)

5. The decision of the U. S. Court of Appeals, the decision of the U. S. District Court in the *Agron* case, and the decision of the U. S. District Court refusing to remand the petitioners suit to the State Court and then dismissing petitioners suit are plainly erroneous on their force because all of these decisions simply ignore the fact that the Federal tax imposed upon the State and City taxes upon phone calls is not authorized by statute and is merely an overcharge by Bell.

CONCLUSION.

For the reasons hereinabove assigned, it is respectfully urged that this Petition for a Writ of Certiorari be granted.

Respectfully submitted,

IRVING GOODMAN

Attorney for Petitioners

APPENDIX.

1.

Opinion of United States Court of Appeals entered September 22, 1971 (not yet reported in Advance Sheets):

IN THE
UNITED STATES DISTRICT COURT
For the Seventh Circuit

SEPTEMBER TERM, 1970 — APRIL SESSION, 1971

No. 71-1022
ROBERT C. AGRON, on behalf of himself and all other telephone subscribers of Illinois Bell Telephone Company who are situated similarly to him,
Plaintiff-Appellant,
v.
ILLINOIS BELL TELEPHONE COMPANY and UNITED STATES OF AMERICA,
Defendants-Appellees.

No. 71-1023
ROBERT C. AGRON, etc.,
Plaintiff-Appellee,
v.
UNITED STATES OF AMERICA,
Defendant-Appellant.

No. 71-1138
ROBERT E. CLEVELAND and FRANCES H. CLEVELAND, on behalf of themselves and all other telephone subscribers and customers of Illinois Bell Telephone Corporation similarly situated,
Plaintiffs-Appellants,
v.
ILLINOIS BELL TELEPHONE COMPANY, an Illinois Corporation, and UNITED STATES OF AMERICA,
Defendants-Appellees.

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division.

September 22, 1971

Before SWYGERT, *Chief Judge*, DUFFY, *Senior Circuit Judge*, and FAIRCHILD, *Circuit Judge*.

SWYGERT, *Chief Judge*. The substantive issue in these three appeals[1] is whether certain occupation taxes imposed on Illinois Bell Telephone Company (IBT) by the State of Illinois and various Illinois municipalities are properly includable in the base on which is computed the federal excise tax on "amounts paid for . . . communication services" under section 4251 of the Internal Revenue Code of 1954. Our resolution of this issue disposes of all three appeals.

Since there was no dispute as to any material fact, the Agron case was determined on cross-motions for summary judgment. Indeed, the case turns wholly on the interpretation and application of various state and federal statutes. The plaintiff, Robert C. Agron, a Chicago resident, is furnished telephone service by IBT. As a telephone subscriber, he is subject to the federal communications tax imposed by section 4251. IBT is required by section 4291 of the Code to collect the federal taxes which are imposed upon its customers, and under section 7501(a) it must hold them in "a special fund in trust for the United States." The amounts collected are paid over to the Internal Revenue Service each month. Treas. Reg. § 49.6302(c)-1. Agron contends that IBT, by including in the federal tax base those amounts identified on his telephone bills as attributable to state and local taxes, has improperly computed the federal tax which it collects from its subscribers and pays over to the United States.[2]

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[1] Pursuant to stipuation, Nos. 71-1022 and 71-1023 were ordered consolidated. By order No. 71-1133 was argued together with Nos. 71-1022 and 71-1023. For convenience, we will defer discussion of No. 71-1138 to the end of this opinion.

[2] Agron's position may be illustrated by reference to a typical telephone bill sent to him by IBT. His January 19, 1967 bill listed the following charges:

	Due to taxes*	U.S. Tax	Total
Telephone service — $17.50	.59	1.81	$19.90

* City and State Taxes.

As can be seen, IBT added the amount attributed to "City and State Taxes" to the basic charge for telephone service and arrived at a base for the federal tax of $18.09. Agron contends that his federal tax should have been $1.75 (10% of $17.50) rather than $1.81 (10% of $18.09).

For years the State of Illinois has imposed a "Messages Tax" on "persons engaged in the business of transmitting messages" which is measured by the "gross receipts from such business." Ill. Rev. Stat. ch. 120, §§ 467.1, 467.2 (1969). This tax was generally imposed at the rate of three percent until 1965 when the rate was increased to four percent. In 1967 the rate was further increased to five percent. In addition to the state tax, IBT is subject to certain local messages taxes. In 1955 Illinois authorized municipalities to tax "Persons engaged in the business of transmitting messages by means of electricity, at a rate not to exceed 5% of the gross receipts from such business originating within the corporate limits of the municipality." Ill. Rev. Stat. ch. 24, § 8-11-2 (1969). Many Illinois municipalities, including the City of Chicago, have exercised this authority to tax IBT.

At the same session at which municipalities were authorized to tax IBT, the Illinois legislature added subsection (a) to Ill. Rev. Stat. ch. 111 2/3, § 36 (1969). That addition provided that whenever a municipality exercised the authority to impose an occupation tax on a utility:

> such utility may charge its customers, in addition to any rate authorized by this Act, an additional charge equal to the sum of (1) an amount equal to such municipal tax, or any part thereof, (2) 3% of such tax, or any part thereof, as the case may be, to cover costs of accounting, and (3) an amount equal to the increases in taxes and other payments to governmental bodies resulting from the amount of such additional charge.

IBT imposes this additional charge by filing a supplemental schedule applicable to the municipality which had imposed the tax. Such a supplemental schedule, if it falls within the legislative authorization cannot be suspended by the Illinois Commerce Commission.[3] Section 36(a) also provides that the additional charge:

[3] When Illinois municipalities have imposed or increased the local messages tax, IBT has almost invariably filed supplemental schedules to recoup the amount of the tax from its customers. On at least one occasion, however, an inadvertent delay in the preparation of a supplemental schedule resulted in IBT's bearing an increased rate of municipal tax for two and one-half months without recouping the amount of the tax from its subscribers.

shall be made by the addition of a uniform percentage to the amounts payable for intrastate utility service in such municipality and shall be shown separately on the utility bill to each customer.

In 1965, when Illinois increased the rate of the state messages tax, the legislature again amended section 36 by adding subsection (b). This addition performed essentially the same function as subsection (a); it authorized tax rate above the prior rate of three percent and provided that IBT could file immediately effective supplemental schedules to recoup any such tax increase.[4]

IBT has computed the federal excise tax which it collects for the government from its customers on a base which includes the separately stated state and local taxes imposed on it. According to Agron this procedure resulted in an overstatement of his federal tax. His efforts to recover the alleged overpayment began in 1967 when he filed a class action against IBT. The suit was eventually dismissed for lack of jurisdiction apparently on the ground that it was essentially a tax refund suit and the jurisdictional requirement of section 7422(a) of the Internal Revenue Code that the taxpayer file a refund claim before bringing such a suit was not complied with. Agron then filed two refund claims, one on behalf of himself individually and another on behalf of himself and all similarly situated subscribers to IBT's services and also on behalf of IBT, and brought the instant suit for refund.

Agron initially named IBT and the United States as defendants in all three counts of his complaint. Count I sought recovery of the amount of Agron's individual tax

[4] Although the additional charge authorized by section 36(b) apparently is not required to be separately stated on the subscriber's telephone bill, IBT has added the amount of the increased state taxes in excess of three percent to the amount of local taxes and has stated the two in one separate category designated as attributable to state and city taxes. Agron seeks recovery only of the amount of federal tax attributable to the inclusion of the separately stated state and local taxes in his federal tax base; he does not contend that the federal tax base should not include the three percent state messages tax which has for many years been imposed on IBT and which although not separately stated, is recouped from IBT's subscribers through rates established after the formal procedure of notice and hearing provided by Ill. Rev. Stat. ch. 111 ⅔, § 36 (1969).

refund claim; Count II asserted a claim for refund of taxes on behalf of a class consisting of all of IBT's subscribers; and Count III sought a refund not only on behalf of all IBT subscribers, but also on behalf of IBT. The Government moved that all three counts be dismissed, but suggested that Count I would state a jurisdictionally sound cause of action if IBT were not joined as a defendant.[5] Agron then voluntarily dismissed IBT from Count I and moved for summary judgment on all three counts. The Government answered Count I and filed a cross-motion for summary judgment on that count while persisting in its claim that the court lacked jurisdiction over Counts II and III. IBT moved for summary judgment on Counts II and III on the ground that it was not a necessary or a proper party.

The district court granted Agron's motion for summary judgment against the United States on Count I[6] and subsequently denied Agron's motion for summary judgment on Counts II and III, ruling in effect that the refund claims filed by the plaintiff on behalf of IBT and the members of the class he purports to represent were not sufficient to satisfy the jurisdictional requirement for maintaining a statutory refund suit. Int. Rev. Code of 1954, § 7422(a). The district court granted Agron judgment for $23.98 against the United States on Count I and dismissed Counts II and III for lack of jurisdiction. Agron appeals the dismissal of Counts II and III and the Government appeals the judgment for Agron on Count I.

We hold that IBT properly computed the federal tax which it collects from its customers and that the district court erred in entering judgment for Agron on Count I. That holding disposes of these appeals and we need not consider the correctness of the district court's order dismissing Counts II and III.

Agron first contends that as a matter of Illinois law, those state and local taxes which are separately stated

[5] The Government's jurisdictional objection to Count I was based on its contention that under 28 U.S.C. § 1346(a)(1), as interpreted in United States v. Sherwood, 312 U.S. 584 (1941), joinder of any other defendant with the United States is impermissible. Accordingly, the dismissal of IBT from Count I removed the alleged jurisdictional defect.

[6] Agron v. Illinois Bell Tel. Co., 319 F. Supp. 418 (N.D. Ill. 1970).

on his telephone bill, while nominally imposed on IBT, are actually direct taxes on telephone subscribers and that his payment of taxes imposed on him by the State of Illinois and the City of Chicago cannot be included in "amounts paid for . . . communication services" under section 4251(a) of the Internal Revenue Code.[7]

The Illinois statutes authorizing and imposing a tax on the occupation or business of transmitting messages by means of electricity are explicit. Ill. Rev. Stat. ch. 120, § 467.2 and ch. 24, § 8-11-2 (1969). For instance, section 467.1 provides that: " 'Taxpayer' means a person engaged in the business of transmitting messages"; and section 467.2 states that: "A tax is imposed upon persons engaged in the business of transmitting messages in this State." It would be difficult to interpret such specific language as imposing a tax on telephone subscribers. It may be that IBT normally "passes on" to its subscribers the economic burden of the state and local occupation taxes[8] just as every unsubsidized business must "pass on" and recover from its customers every item of operating expense—including state and federal taxes—if it is to operate profitably.[9] But the fact that the telephone subscriber ultimately bears the financial burden of the tax does not justify our ignoring the clear language of the Illinois statutes and holding that the tax is "imposed" on subscribers.

---

[7] We have assumed, with Agron, that if the state and local taxes in question were actually direct taxes imposed on telephone subscribers, then amounts attributable to those taxes could not be considered "amounts paid for . . . communication services." Because we hold that the State of Illinois does not consider its state and local taxes to be direct taxes on subscribers, we need not reach and do not decide that question.

[8] However, as we pointed out in note 6, supra, on at least one occasion IBT was forced to bear an increased rate of municipal tax for two and one-half months. Agron does not suggest that IBT's failure to "pass the tax on" to its subscribers in any way affected its liability to pay the tax.

[9] Cf. FPC v. United Gas Pipe Line Co., 386 U.S. 237, 243 (1967); and Galveston Elec. Co. v. Galveston, 258 U.S. 388, 399 (1922). In those cases the Supreme Court stated that an allowance for taxes should be included in determining regulated utilities' expenses for purposes of fixing rates which will provide a fair return. Thus the economic burden of the federal taxes is "passed on" to consumers but that does not result in the taxes' being "imposed" on consumers.

The decisions of the Illinois Supreme Court make clear that it is the privilege of carrying on certain businesses within the state that the legislature intended to tax in enacting the occupation taxes. *See, e.g., People's Drug Shop, Inc.* v. *Moysey,* 384 Ill. 283, 285-87, 51 N.E. 2d 144, 146 (1943). In *Reif* v. *Barrett,* 355 Ill. 104, 109, 188 N.E. 889, 892 (1933),[10] the court stated that the purpose of an occupation tax is:

> [E]ither to regulate and control a given business or occupation, or to impose a tax for the privilege of exercising, undertaking or operating a given occupation, trade or profession. Its effect is to license a person engaged in a given calling or occupation. A license in form may not be issued to a taxpayer but the payment of the tax is the license under the authority of the State to engage in such occupation.

Thus it is apparent that Illinois has not considered its occupation taxes to be direct taxes on consumers.

Even though the economic burden of the occupation taxes is "passed on," the Illinois courts have consistently ruled that such taxes are not imposed on consumers. In *Winter* v. *Barrett,* 352 Ill. 441, 455-56, 186 N.E. 113, 120-21 (1933), the court rejected the argument that the state tax on those engaged in the business of selling personal property at retail was imposed on consumers. The court pointed out that retailers could take the tax into consideration in fixing the selling price of their goods, "the same as they do their property taxes, rent and other expenses of doing business"; but the court held that the tax remained on the seller and that the seller must report and pay tax on the full amount he receives for his property, including any amount added to the price to compensate for the tax. *See also Vause & Striegel, Inc.* v. *McKibbin,* 379 Ill. 169, 173, 39 N.E.2d 1006, 1008 (1942). The Illinois Supreme Court used the same reasoning to reject an analogous argument by a liquor retailer who contended that federal and state taxes nominally imposed on distillers were actually "passed on" to retailers and ultimately to consumers and that amounts attributable to those taxes could not be included in gross

[10] Reif v. Barrett, insofar as it held that the Illinois Constitution limited the legislature to property taxes, occupation taxes and franchise or privilege taxes, was overruled by Thorpe v. Mahin, 43 Ill. 2d 36, 45, 250 N.E. 2d 633, 637 (1969). See n. 11, supra.

receipts subject to the occupation tax on retailers. *Fischman & Sons, Inc.* v. *Department of Revenue*, 12 Ill. 2d 253, 146 N.E.2d 54 (1957). *See also People* v. *Werner*, 364 Ill. 594, 5 N.E.2d 238 (1936). A three-judge federal district court has followed the Illinois courts in ruling that the Illinois Retailers' Occupation Tax—even if passed on—is not imposed on consumers. *United States* v. *Department of Revenue*, 202 F. Supp. 757 (N.D. Ill.), *aff'd per curiam*, 371 U.S. 21 (1962).

Even if the language of the Illinois statutes and court decisions were less clear, a further bar exists to our accepting Agron's argument that the state and local occupation taxes are imposed on consumers. For many years the Illinois Supreme Court consistently ruled that the state constitution, art. IX, § 1, limited the legislature to three forms of taxation: (1) property taxes on a valuation basis, (2) occupation taxes, and (3) franchise or privilege taxes.[11] This restrictive interpretation of the state constitution was recently disavowed by *Thorpe* v. *Mahin*, 43 Ill. 2d 36, 42-45, 250 N.E.2d 633, 636-37 (1969); but the tax on IBT was obviously intended, when enacted, to fall within the constitutional authorization of taxes on occupations. We may not ignore the obvious intention of the Illinois legislature and rule that this occupation tax is a direct tax on consumers. Further, the title of the state taxing statute applicable to IBT is, "An Act in relation to a tax upon persons engaged in the business of transmitting messages"; and under art. IV, § 13 of the state constitution, no tax may be imposed upon persons not described in the title of the taxing statute. *See, e.g., International Business Machines Corp.* v. *Department of Revenue*, 25 Ill.2d 503, 185 N.E.2d 257 (1962). *Cf. Central*

[11] See, e.g., Reif v. Barrett, 355 Ill. 104, 110, 188 N.E. 889, 893 (1933); Bachrach v. Nelson, 349 Ill. 579, 589, 182 N.E. 909, 913 (1932). Only recently has the Illinois Supreme Court, in upholding the state income tax, Ill. Rev. Stat. ch. 120, § 1-101 (1969), overruled Reif and Bachrash and held that Ill. Const. art. IX, § 2, broadened the forms of taxation beyond those stated in art. IX, § 1. Thorpe v. Mahin, 43 Ill. 2d 36, 42-45, 250 N.E. 2d 633, 636-637 (1969). Even then, the court referred to the tax as one on the privilege of receiving income, 43 Ill. 2d at 45, 250 N.E. 2d at 638.

We note that Illinois recently adopted a new constitution generally effective July 1, 1971. However, the new constitution is not relevant to our interpretation of statutes passed many years ago under the old constitution.

Television Serv. Inc. v. *Isaacs*, 27 Ill.2d 420, 189 N.E.2d 333 (1963).[12]

Agron's argument that the occupation tax on IBT is imposed on him and other telephone subscribers rests entirely on certain language in a recent case, *East St. Louis* v. *Union Elec. Co.*, 37 Ill.2d 537, 542-43, 229 N.E.2d 522, 525 (1967), *cert. denied*, 390 U.S. 948 (1968), to the effect that the burden of a certain municipal occupation tax fell directly on consumers:

> On a literal and superficial view it might appear as if the utility tax ordinance imposed a tax burden upon the Company, but on examination it is evident that the burden was placed on the consumers. The Company as authorized simply passed on the new charges to its consumers and the consumers not only paid such charges to the City but also paid the Company the expenses it incurred while serving as a collector or conduit of taxes from the consumers to the City.

The district court accepted Agron's argument and, relying on *East St. Louis*, ruled that "Illinois does not consider these amounts on the telephone bill due to state and local taxes to be levies on the company, but, rather, charges on the telephone subscriber." 319 F. Supp. at 421. We disagree. *East St. Louis* involved the construction of a 1948 municipal ordinance which granted the Union Electric Company the right to operate its distribution system within the City of East St. Louis. In return, the company agreed to pay annually the amount by which certain percentages of its gross receipts exceeded all other payments to the city for "fees, licenses, charges, taxes or other exactions . . . imposed by any valid ordinance of the City of East St. Louis." In 1960 when the city imposed a municipal occupation tax on the company, a controversy developed over whether the occupation tax was a "tax" within the 1948 franchise ordinance. If it were, the electric company would have had no further liability for franchise payments. The company, although it passed on the occu-

[12] A municipal tax upon persons not described in the authorizing statute is also void. Cf. Wabash R.R. v. Department of Revenue, 28 Ill. 2d 128, 191 N.E. 2d 244 (1963).

pation tax to its customers, refused to make further franchise payments and asserted that to require it to do so would unconstitutionally impair its franchise contract with the city.

The question before the Illinois Supreme Court was whether an occupation tax which imposed no additional economic burden on the electric company fell within the intendment of "taxes" as expressed in the city's 1948 ordinance. Relying on the rule that, "A state or ordinance must receive a sensible construction, even though such construction qualifies the universality of its language," *Elmhurst* v. *Buettgen*, 394 Ill. 248, 253, 68 N.E.2d 278, 282 (1946), the court held that the company's liability for the occupation tax did not discharge its obligation to make franchise payments.

East St. Louis does not support the district court's ruling since it merely recognized the economic reality that the ultimate consumer bears the burden of all prior taxes imposed on those from whom he receives goods or services. That case held only that the parties did not intend in 1948 that the imposition in the future of a tax which imposed no burden on the electric company would discharge its obligations under the franchise ordinance. We agree with the Government that the Illinois Supreme Court could hardly have intended by its decision to rewrite whole sections of the statutes and ordinances imposing occupation taxes on utilities.

From the foregoing, we conclude that the statement of the Illinois Supreme Court in *People's Drug Shop, Inc.* v. *Moysey*, 384 Ill. 283, 287, 51 N.E.2d 144, 146 (1943), concerning the Retailers' Occupation Tax is applicable to the state and local occupation taxes presently imposed on IBT: "Unambiguous provisions of the . . . Act proclaim, and the decisions of this court uniformly hold, that the tax imposed is upon retailers and not upon consumers, and that the sole duty of paying the tax rests upon the former."

Agron next contends that even if separately stated state and local messages taxes are not directly "imposed" on telephone subscribers, they are, nevertheless, identified as taxes and ought not be considered a charge for tele-

phone service within the meaning of section 4251(a) of the Internal Revenue Code. The Government counters that the additional charge is merely part of the compensation demanded by IBT for furnishing the service of transmitting messages; thus, amounts paid to reimburse IBT for its payment of the state and local messages taxes—just as amounts paid to reimburse IBT for all other taxes and for labor costs and equipment repairs—are paid for telephone service within the meaning of the statute. We agree with the Government. All costs incurred in making a product or service available—including the cost of federal, state and local taxes—are ultimately borne by consumers. That the cost of taxes imposed on manufacturers and retailers is added into the price at which goods are sold, even if such taxes are itemized and specifically identified, simply increases the price the consumer must pay to receive the goods or services.

Additional charges contained in supplemental schedules filed by IBT under Ill. Rev. Stat. ch. 111 ⅔, §§ 36(a) and 36(b) (1969), even though in economic terms they result in the passing on of the burden of state and local messages taxes to subscribers, are simply a part of the price such subscribers must pay to IBT to receive telephone service.[13] Agron argues that the additional charges are not a part of IBT's price for its services because these charges are not authorized by rate schedules arrived at independently by the Illinois Commerce Commission after notice and hearing. We deem this fact to be without significance. The additional charges were authorized by the Illinois legislature which, in enacting sections 36(a) and (b) of Ill. Rev. Stat. ch. 111 ⅔ (1969); was not imposing a tax on consumers or creating a new type of charge for utility service but was simply providing a convenient, efficient procedure by which IBT could bypass the costly administrative rate-making procedure and obtain minor increases in the authorized rate for its services.

[13] Perhaps it might also be argued that even direct federal, state and local taxes of subscribers are a part of the "price" those subscribers must pay to receive telephone service. But that simply illustrates the extent to which the problem presented by this case is one of semantics; it does not change our view that amounts IBT demands, under schedules authorized by Illinois law, as reimbursement for taxes it pays are as much a part of its price for its services as amounts reimbursing it for labor or equipment costs.

In his attempt to show that the additional charges collected by IBT are not a part of the price for telephone service, Agron argues that persons living in cities which have not imposed a local tax on IBT receive the same service at a lower price than persons living in cities where a local tax on IBT is in effect. For example, according to Agron, the basic charge for a three minute call between Chicago and Lincoln, Illinois, is $1.00. Using Agron's figures, if the call originates in Lincoln, the total charge is $1.10—$1.00 plus ten cents federal tax; however, if the call originates in Chicago, the total charge is $1.16—$1.00 plus five cents local tax, plus eleven cents federal tax. Agron concludes that the Chicagoan is required to pay ten percent more federal tax for the identical service because of the inclusion of Chicago's separately stated local tax in the determination of the charge for the service. Agron has failed to recognize, however, that Chicago, by imposing a municipal tax on IBT, has increased the cost of IBT's doing business within the city with the consequence that Chicago residents must pay more *for telephone service* to provide IBT a fair return. Since the federal tax is based on "the sum of all charges for . . . [telephone] services included in the [consumer's] bill," it follows that the amount of federal tax which Chicago residents must pay would increase;[14] and neither IBT nor the

[14] The Government places much reliance on the fact that Congress provided that the tax be computed on "the sum of all charges." We agree that that language indicates a general congressional intention that the amount charged by a telephone company should not be broken down into its component parts for purposes of computing the tax. For instance, it is clear that no attempt should be made to separate out the amounts attributable to taxes, of whatever kind, which were considered by the Illinois Commerce Commission in fixing IBT's general rate structure. Agron concedes this by his failure to seek recovery of any taxes attributable to the inclusion in the federal tax base of amounts which IBT receives as reimbursement for its payment of that part of the state messages tax (the initial three percent) which is not separately stated.

However, Agron correctly points out that the "sum of all charges" language does not itself solve the problem presented in these appeals; for it is only the sum of all charges for telephone service which is subject to tax. The Government appears to concede that not every charge which might be contained in a telephone bill should be included in the federal tax base. For instance, amounts paid by telephone subscribers in order to be listed in "yellow page" directories are considered payments for advertising rather than for telephone service and are not subject to the federal tax. See Revenue Ruling 58-299, 1958-1 Cum.

State of Illinois can defeat that result by providing for the itemization, of those amounts passed on to consumers which are attributable to taxes on IBT. *Cf. Vause & Striegel, Inc.* v. *McKibbin*, 379 Ill. 169, 173, 39 N.E.2d 1006, 1008 (1942).

In *Lash's Products Co.* v. *United States*, 278 U.S. 175 (1929), the Supreme Court was faced with an argument essentially identical to that made by Agron. There, a manufacturer, who was subject to a federal tax computed on the price at which he sold certain products and who had notified his customers that the price of his products reflected his tax liability, argued that amounts which he received from his customers to reimburse him for his obligation to pay the federal tax were not a part of the "price" of his products and could therefore not be included in the base on which the federal tax was computed. In effect, the manufacturer argued, as does Agron here, that amounts attributable to his tax liability were not charges for the product but were for taxes. The language of the Supreme Court in rejecting the manufacturer's argument, 278 U.S. at 176, is equally applicable to Agron's claim:

> [T]he tax is laid and remains on the manufacturer and on him alone. . . . The purchaser does not pay the tax. He pays or may pay the seller more for the goods because of the seller's obligation, but that is all.
>
> • • •
>
> The price is the total sum paid for the goods. The amount added because of the tax is paid to get the goods and for nothing else. Therefore it is part of the price. . . ."[15]

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[14] (Continued)
Bull. 436; cf. Revenue Ruling 68-92, 1968-1 Cum. Bull. 488. Thus the crux of the problem before us remains whether the additional charge stated on IBT's bills is an increase in the price for telephone service resulting from IBT's liability for the state and local occuptaion tares.

[15] Cf. James v. Dravo Contracting Co., 302 U.S. 134, 160 (1937); Dow Jones & Co. v. United States, 128 F. Supp. 748 (Ct. Cl. 1955); Sun Oil Co. v. Gross Income Tax Div., 238 Ind. 111, 149 N.E. 2d 115 (1958); Fischman & Sons, Inc. v. Department of Revenue, 12 Ill. 2d 253, 146 N.E. 2d 54 (1957); Hoffman v. City of Syracuse, 2 N.Y. 2d 484, 141 N.E. 2d 605 (1957); People v. Werner, 364 Ill. 594, 5 N.E. 2d 238 (1936). These cases recognize that increases in the amount a purchaser must pay for goods or services in order to compensate the seller for taxes imposed on him or on those from whom he purchased the goods are a part of the "price" of the foods themselves. The prior taxes merely increase the cost of the goods.

Applying the Court's reasoning to Agron's argument, we conclude that even though the additional charges imposed on Agron and other telephone subscribers may be directly attributable to state and local taxes paid by IBT, those additional charges are nonetheless a part of the price IBT demands for its services. Accordingly, they are properly includable in the base on which the federal tax on "amounts paid for . . . communication services" is computed.

In sum, we conclude that the procedure by which IBT computes and collects the tax imposed by section 4251 of the Internal Revenue Code does not result in any over-assessment of the federal tax and that the district court erred in granting a tax refund to Agron. This holding renders moot the issues presented by Agron's appeal. Since we hold that there was no underlying cause of action on which a class suit could be based, we need not reach the procedural problems raised by Agron's attempting to bring a class or derivative action for tax refund, and we intimate no opinion on the correctness of the district court's dismissal of Counts II and III.

Our ruling on the merits of Agron's claim also disposes of the Clevelands' appeal. Their original complaint was filed in the Circuit Court of Cook County on behalf of themselves and all similarly situated IBT subscribers. That suit was against IBT alone and alleged the same improper computation of federal tax as was asserted by Agron. After removal of the federal district court, the plaintiffs filed an amended complaint naming the United States as defendant with IBT. Both defendants sought dismissal of the complaint on the ground, among others, that the plaintiffs had failed to file an administrative refund claim as required by section 7422(a) of the Internal Revenue Code. The district court granted the dismissal.

The Clevelands rely on essentially the same facts as those presented by Agron but urge a different legal theory. They argue that their suit is not for refund of taxes and that their dispute is solely with IBT, whom they contend has overcharged its customers without authority under either federal or state statute. They argue that,

accordingly, the United States need not be a party and that the filing of an administrative tax refund claim is not a prerequisite to their bringing suit.

Because we hold that IBT properly computed the federal tax in accordance with the provisions of the Internal Revenue Code, the underlying basis of the Clevelands' complaint falls and therefore we need not decide whether the Clevelands should have been required to file an administrative tax refund claim or who, as between IBT and the federal government, might be liable for any alleged overcharge.

The order granting Agron's motion for summary judgment and denying the Government's motion for summary judgment as to Count I of Agron's complaint is reversed; the order dismissing the Clevelands' complaint is affirmed; and Agron's appeal from the dismissal of Counts II and III of his complaint is dismissed as moot.

2.

Opinion of United States District Court in case of Agron v. Illinois Bell & United States, No. 69 C 1971 handed down October 16, 1970, and reported in 319 F. Supp. 418:

MAROVITZ, *District Judge*

MEMORANDUM OPINION

Cross-motions for Summary Judgment on Count I

This is an action for the refund of certain federal excise taxes on telephone service alleged to have been overpaid since and including the last quarter of 1965. In addition to the alleged overpayments or overcollections, depending on one's view, plaintiff seeks statutory interest.

The Complaint consists of three counts: Count I, brought by Robert C. Agron, a subscriber to the telephone services of the Illinois Bell Telephone Company

(IBT), against the United States raises the narrow, if perplexing, legal issue of the taxability of certain amounts set forth of plaintiff's telephone bill. Count II is brought as a class action by plaintiff on behalf of all telephone subscribers similarly situated. The Illinois Bell Telephone Company is joined as a defendant in this count. Count III is brought not only on behalf of all IBT subscribers, but also on behalf of IBT. Presently pending before this Court are cross-motions for summary judgment on Count I, IBT's motions for summary judgment on Counts II and III, and the Government's motions to dismiss Counts II and III. While Counts II and III raise jurisdictional and procedural questions, the ultimate substantive issue in all counts, the propriety of the challenged federal tax on telephone service, is the same. We turn now to the cross-motions for summary judgment on Count I. "(S)ummary judgment is appropriate where, as here, there are no material factual issues in dispute and only legal issues need be resolved. *Chicago Joint Board* v. *Chicago Tribune Co.*, 307 F. Supp. 422, 424 (N.D. Ill. 1969).

The Government, under 26 U.S.C. § 4251 (a), imposes a communications excise tax on persons who pay for local toll telephone service. Local and toll telephone service is defined in the following section, 26 U.S.C. § 4252 (a,b). Telephone companies such as IBT, are required to collect the federal communications tax imposed on their subscribers under Section 4251. 26 U.S.C. § 4291.

The State of Illinois also imposes taxes on telephone companies engaged in transmitting messages. Ill. Rev. Stats., Ch. 120, § 467.2 (1969). The companies are au-

thorized to pass a portion of that tax on to their subscribers or customers. Ill. Rev. Stats., Ch. 111⅔, § 36 (b). Similarly, some local municipalities impose a tax on telephone companies. Ill. Rev. Stats., Ch. 24, § 8-11-2 (1969), which charge may also be passed on to customers. Ill. Rev. Stats., Ch. 111⅔, § 36 (b) (1969).

On its bills to its customers, the IBT separately lists the amount due on account of state and local taxes. See Complaint, Ex. 2 to Ex. 1. The Government, through the IBT as its collector or conduit, has been collecting its communications services tax, currently at the rate of 10%, on the total of the charges set forth by both telephone service and state and local taxes. For instance, one IBT bill sent to plaintiff provided in part:

		Due to Taxes*	U. S. Tax	
Telephone service	17 50	59	1 81	19 90

* City and state taxes

The narrow substantive issue before the Court is whether the federal communications tax is properly imposed. Plaintiff claims that the amount on his bill "due to taxes" is not an amount paid "for communication services," pursuant to 26 U.S.C., §4251 (a), that, basically, he is being taxed on a tax, and that, consequently, the amounts attributable to state and local taxes should be excluded from consideration when the federal excise tax is calculated. Essentially, the Government's position is that the various state and municipal taxes are imposed on the telephone companies and not on telephone customers, that these items are just like any other operating expenses, and that they may be passed on to the customers as a charge for communications services.

The federal excise tax is imposed on "amounts paid for the following communications services . . .:

> Local telephone service.
> Toll telephone service.
> . . ."

26 U.S.C. §4251 (a) (1). Both parties agree that the terms local and toll telephone service are to be given "their commonly accepted and understood meaning—the right to use a telephone which is part of a telephone system and to communicate thereby with other persons having telephones which are part of this system." Now 26 U.S.C. § 4254 (a) provides that "(i)f a bill is rendered the taxpayer for local telephone service or toll telephone service—

> (1) the amount on which the tax with respect to such services shall be based shall be the sum of all charges for such services included in the bill . . ."

Again, plaintiff claims that the federal tax is on the cost of telephone services only and not on local or state taxes on those services. The Government suggests that the challenged amounts are another kind of charge for such services which charge may be used as a basis for calculating the federal tax due.

A key to this puzzle can be found in the construction of the Illinois statutes which concern telephone taxes. As noted previously, "persons engaged in the business of transmitting messages in" Illinois, e. g., telephone companies, are assessed a "gross receipts" tax. Ill. Rev. Stats., Ch. 120, § 467.2 (1960), which tax may be passed on to their customers, Ill. Rev. Stats., Ch. 111⅔ § 36 (b) (1969). Confronted with interpreting parallel statutory provisions which ostensibly taxes public utilities such

as electric companies and permitted them to pass the charges on to their customers, the Illinois Supreme Court said in *East St. Louis* v. *Union Electric Co.*, 37 Ill. 2d 537, 542-43 (1967):

> "On a literal and superficial view it might appear as if the utility tax ordinance imposed a tax burden upon the Company, but on examination it is evident that the burden was placed on the consumers. The Company, as authorized, simply passed on the new charges to its customers and the consumers not only paid such charges to the City but also paid the Company the expenses it incurred while serving as a collector or conduit of taxes from the consumers to the City."

Essentially, then, the Illinois Supreme Court found that the statutory assessments were tantamount to or functionally equivalent to direct taxes on the consumers because the consumers were authorized to be charged, were charged, and, in fact, paid the amount due, plus an extra portion to cover the cost of collection. Significantly, the companies absorbed no collection costs. *Id.*

The state and local telephone tax system is indistinguishable from the utilities tax system construed in the *East St. Louis* case. Based on that case, there is no doubt that Illinois does not consider those amounts on the telephone bill due to state and local taxes to be levies on the company, but, rather, charges on the telephone subscriber. Under this construction, the amounts are not charges for local or toll telephone service under federal law. Consequently, they ought not be considered in that basis from which the federal telephone excise tax is figured.

Both sides make numerous references to former and current tax regulations which purport to clarify the lan-

guage of the internal revenue statutes. We are frank to say those regulations basically are wordy exercises in circular reasoning which, in the final analysis, add little or nothing to an understanding of the problem before this Court.

We find, then, that the amount on plaintiff's telephone bill which is separately listed as due to taxes is not a charge for telephone services, but rather, an assessment which is based on the telephone company's charge for service. Moreover, this assessment is, in reality, levied against the telephone subscriber or consumer. Thus, the federal telephone excise tax may not be based, to any extent on this amount. Summary judgment on Count I of the Complaint is granted to plaintiff and denied to the Government.

3.

Copy of Opinion of United States District Court in Agron v. Illinois Bell and United States, No. 69 C 1972 handed down December 11, 1970 and reported in 325 F. Supp. 487:

MARKOVITZ, *District Judge,*

MEMORANDUM OPINION

Cross-Motions for Summary Judgment

This is an action for the refund of certain federal excise taxes on telephone service. The Complaint consists of three counts. Count I was brought by Robert C. Agron, a subscriber to the telephone services of the Illinois Bell Telephone Company (IBT), against the United States, and challenged the legality of the assessment of federal telephone excise taxes on that portion of a subscriber's telephone bill which is attributable to state and local

taxes. On October 16, 1970, this Court granted summary judgment to plaintiff and against the Government, holding that assessments due to state and local taxes could not be considered in that basis from which the federal telephone excise tax was calculated, 319 F. Supp. 418. Count II of the Complaint is brought on behalf of all telephone subscribers similarly situated. IBT is joined as a defendant in this count. Count III is brought not only on behalf of all IBT subscribers, but also on behalf of IBT. Presently before the Court are the Government's motion to dismiss Counts II and III, IBT's motion for summary judgment on Counts II and III, and plaintiff's motion for a class action determination and for summary judgment on Counts II and III.

[1] While extensive and involved briefs have been submitted by all parties, the complete, if short, answer to the basic issue raised in Count II is that plaintiff's class action for tax refunds may not be maintained. An action for the refund of federal taxes may only be commenced after an administrative claim has been filed and disallowed. 26 U.S.C. § 7422(a); *United States* v. *Wells Fargo Bank*, 393 F. 2d 272, 273 (9th Cir. 1968); *Mulcahy* v. *United States*, 388 F. 2d 300, 302 (5th Cir. 1968); *England* v. *United States*, 261 F. 2d 455, 456 (7th Cir. 1958). Plaintiff has not alleged that any, much less all, of the tens of thousands of claimants on whose behalf he allegedly brings this action have exhausted their available administrative remedies. Plaintiff does allege that he filed and administrative tax refund claim on behalf of himself and all telephone subscribers similarly situated and that said claim was rejected. Complaint ¶ 23,

Ex. 4. We find that attempt at satisfying the administrative prerequisites to this kind of civil suit to be unsatisfactory. By failing to name the claimants and the amounts due to each, plaintiff's claim on their behalf falls far short of the detail required by federal regulations. 26 C.F.R. § 301.6402-2. See *Herrington* v. *United States*, 416 F. 2d 1029, 1031-1032 (10th Cir. 1969).

[2] Essentially, an unauthorized agent may not "claim an unspecified refund for unknown principals." *Hankins* v. *United States*, 66-2 U.S.T.C. ¶ 9543, at 86,702 (E.D. Okla. 1966), aff'd. on other grounds, 375 F. 2d 239 (10th Cir. 1967). Consequently, the only party of whom we are aware that has standing to bring this action under 28 U.S.C. § 1346(a) (1), is the named plaintiff, Agron, who, at best, may be said to constitute a class of one. *McConnell* v. *United States*, 295 F. Supp. 605, 606 (E.D. Tenn. 1969); *Lipset* v. *United States*, 37 F.R.D. 549, 551-552 (S.D. N.Y. 1965), appeal dismissed, 359 F. 2d 956 (2d Cir. 1966).

[3] Once the class aspects of Count II are disregarded, the only difference between it and Count I is that IBT is named as a party defendant. IBT was allegedly joined as a party defendant under Rule 19, F.R.Civ.P., because it was needed for a just adjudication. Complaint, ¶ 20. The Government persuasively contends that the attempted joinder of a private litigant in a tax refund action is improper. See 28 U.S.C. § 1346 (a) (1); 26 U.S.C. § 7422(f); *Lazier* v. *United States*, 77 F. Supp. 241, 243 (D. N.D. 1948); *DeVan* v. *United States*, 50 F. Supp. 992, 995 (D. N.J. 1943); see also, *United States* v. *Sherwood*, 312 U.S. 584, 588, 61 S. Ct. 767, 85 L. Ed. 1058 (1941); *Berkeley* v. *United States*, 276 F. 2d 9, 12, 149 Ct. Cl. 549 (1960).

Since the relief to which plaintiff is entitled may occur without the involvement of IBT, the company is obviously not necessary in order to achieve a just adjudication. In view of this fact and the rules dealing with the relevant joinder in question, IBT ought to be and is hereby dismissed as a party defendant in Count II.

Summarizing, this Court finds that the only party entitled to bring this action is the named plaintiff, Agron, and that summary judgment is granted to both defendants and denied to plaintiff as to Count II.

[4] Count III is in the nature of a class derivative action brought on behalf of IBT, plaintiff's theory being that IBT breached its fiduciary duty to the class to prevent its subscribers from being overcharged. Much of what has already been stated with respect to propriety of Count II applies here as well. In addition, since the challenged federal tax, 26 U.S.C. § 4251, is imposed on telephone customers, not companies, IBT had no claim to press against the Government. It was not the person assessed, nor was it the authorized agent of such a person, 26 C.F.R. § 301.6402-2(e). Neither was IBT eligible to pursue a claim under 26 U.S.C. § 6415(a) which permits tax collectors to obtain credits or refunds under certain circumstances not alleged to be present in the instant action. The obligation which IBT was bound to perform was not litigation on behalf of its subscribers, but the collection and holding of certain tax revenues according to federal statutes, 26 U.S.C. §§ 4291, 7501(a), and policy. In short, IBT has no corporate claim to press, so there are no shoes in which plaintiff can stand. See *Agron* v. *Illinois Bell Telephone Co.*, 67 C 2041 (N.D. Ill. Aug. 4, 1969), per Napoli, J. Defendants are entitled to summary judgment on Count III.

4.

Opinion and Order of United States District Court in Cleveland v. Illinois Bell, Case No. 69 C 2171 (not reported) refusing to remand cause to the State Court:

MEMORANDUM OPINION filed by Judge Marovitz Denying Plaintiffs' Motion to Remand, filed December 12, 1969:

MEMORANDUM OPINION

Plaintiffs' Motion to Remand

Originally brought in state court, this is an action which alleges that defendant Illinois Bell Telephone Company has wrongfully overcharged plaintiff telephone subscribers and customers. Plaintiffs, who bring this action on behalf of themselves and all those similarly situated, are seeking declaratory and injunctive relief as well as a refund of the money improperly collected. Following the removal of this action from the state court to the federal court, 28 U.S.C. § 1441(b), the plaintiffs filed a motion to remand, 28 U.S.C. § 1447(c).

The party requesting for removal has the burden of proving entitlement. *Pan American Pharmaceutical, Inc.* v. *Sherman Laboratories, Inc.*, 293 F. Supp. 713, 717 (D. P.R. 1968). Further, we note that removal statutes are to be construed strictly, with doubtful cases resolved against removal. *Barnett* v. *Faber, Coe & Gregg, Inc.*, 291 F. Supp. 178, 180 (S.D. N.Y. 1968); *Couch* v. *White Motor Co.*, 290 F. Supp. 697, 699 (W.D. Co. 1968). Should it appear that any case was removed improvidently, the federal court must remand it. 28 U.S.C. § 1447(c).

Civil actions are removable without regard to diversity of citizenship if the federal court has original federal

question jurisdiction. 28 U.S.C. § 1441(b). That is, for proper removal pursuant to this section, the claim or right asserted must arise under the Constitution, treaties or laws of the United States.

> "The federal nature of the claim must appear from consideration of the complaint alone and the claim must be one that is essentially federal; the presence of federal defenses will not operate to confer federal jurisdiction." *Denver Union Stock Yard Co.* v. *Litvak Meat Co.*, 295 F. Supp. 809, 810 (D. Col. 1968).

The pertinent allegations set forth in the instant complaint are that plaintiffs are customers of the defendant telephone company, that there exists a ten per cent (10%) federal excise tax on communication services pursuant to 26 U.S.C. §§ 4251-54, that Section 4254 establishes as the basis against which the tax is assessed "the sum of all charges for such (telephone) services included in the bill . . .," that the telephone company, in determining the amount of excise tax due to the United States, includes in base figure amounts equivalent to various state and local taxes imposed on telephone service, that state and municipal taxes are not proper charges to be included in determining the federal tax base, and that, consequently, the assessment made by the defendant constitutes an "overcharge" or a "tax upon a tax" which is "contrary to the intent of the United States statute hereinbefore referred to . . ." and is otherwise unfair, arbitrary and unconstitutional, thereby entitling plaintiffs to a refund. Complaint, ¶¶ 1-3, 6, 8.

It does not appear that any factual dispute is present or will develop in this case. There is no doubt that the defendant telephone company assesses a federal excise

tax on an amount which includes, in addition to the monthly service charge and a charge for extra call units, a separate charge for state and city taxes. Complaint ¶ 4, Exhibits A-F.

The legal issue presented is a very narrow one, namely, whether or not certain state and local taxes on telephone service are charges includible in determining the amount upon which the federal communications tax is imposed. If so, plaintiffs' action fails. If not, plaintiffs may prevail.

Thus, the resolution of the instant dispute hinges on not just substantially, but entirely, on a construction of a federal statutory scheme. *Cf. Columbia Pictures Corp.* v. *Towne Theatre Corp.*, 282 F. Supp. 467, 469 (E.D. Wis. 1968). The federal law is cited and quoted in the plaintiffs' complaint. A specific allegation is made to the effect that defendant's assessment is contrary to the intent of the law. Federal law, then, is a real, substantial, and essential element of the plaintiffs' case, sufficiently central to affect the outcome. *Urban Renewal Authority of City of Trinidad, Colo.* v. *Dougherty*, 271 F. Supp. 729, 732-33 (D. Col. 1967); *Sylgab Steel & Wire Corp.* v. *Strickland Transp. Co.*, 270 F. Supp. 264, 267-68 (E.D. N.Y. 1967); *Chambers-Liberty Counties Nav. Dist.* v. *Parker Bros. & Co.*, 263 F. Supp. 602, 606 (S.D. Tex. 1967).

The plaintiffs have suggested that removal was improper because the United States was not a party to the suit and because the action is not one for refund of taxes from the United States, but, rather, for refund of monies wrongfully assessed by the defendant. First, federal question jurisdiction is not dependent upon the parties to

the lawsuit, but only upon the subject matter presented by the complaint. Next, to say that this action is not brought for a refund of taxes or that the United States is not charging the tax is absurd because, as the complaint alleged, the money was assessed pursuant to federal law regarding communication taxes; 28 U.S.C. §§ 4251-54. Moreover, the defendant in so assessing and collecting the tax was acting as the agent for the federal government, 28 U.S.C. § 4291. See also 26 U.S.C. § 7501 (a); Treas. Reg. § 49.6302(c)-1 (1968).

In contrast to two other cases where a removed case was remanded, *New Jersey* v. *Moriarty,* 268 F. Supp. 546 (D. N.J. 1967) and *Meyerhoff* v. *Garten,* 232 F. Supp. 363 (D. Md. 1964), the instant case involves only federal law and the rights asserted and the relief demanded depend solely upon an interpretation of the phrase "sum of all charges" found in 28 U.S.C. § 4254. Consequently, we find that this court does have original jurisdiction over the claims presented in the complaint and that the case was not improvidently removed.

The plaintiffs' motion to remand is denied.

Enter: /s/ Abraham L. Marovitz

5.

Opinion and Order of United States District Court in Cleveland v. Illinois Bell and United States, Case No. 69 C 2171 (not reported):

ORDER DISMISSING SUIT

This cause coming on to be heard upon the Amended and Supplemental Complaint filed by the Plaintiffs on behalf of themselves and all telephone subscribers and

customers of Illinois Bell Telephone Company similarly situated, and upon the motion to dismiss filed by the United States of America, Defendant, and upon the answer filed by the Defendant, Illinois Bell Telephone Company, an Illinois corporation, and upon the petition of the Plaintiffs for an order to consolidate the above entitled with the cause entitled "Robert C. Agron, etc. vs. Illinois Bell Telephone Company, an Illinois corporation and United States of America, No. 69 C 1972" pending in the United States District Court, and the Court having heard the arguments of respective counsel and having read the briefs filed by the various parties hereto, and the Court being fully advised in the premises;

It Is Ordered that the motion to dismiss filed by the United States of America be and the same is hereby allowed, and the above cause is hereby dismissed against the United States of America at Plaintiffs' cost.

It Is Further Ordered that the Court having read the answer filed by the Defendant, Illinois Bell Telephone Company, an Illinois corporation, that the above cause be and is dismissed as to the Defendant, Illinois Bell Telephone Company, an Illinois corporation, at Plaintiffs' cost.

It Is Further Ordered that the amended and supplemental complaint heretofore filed by the Plaintiffs in the above entitled cause be and is dismissed in its entirety at Plaintiffs' cost.

It Is Further Ordered that the petition of the Plaintiff to consolidate the above entitled cause with the case entitled "Robert C. Agron, etc. vs. Illinois Bell Telephone Company, an Illinois Corporation and United States of

America, No. 69 C 1972, be and the same is hereby denied, the matter having become moot as a result of the order entered by this Court this day in the cause entitled Robert C. Agron, etc. vs. Illinois Bell Telephone Company, et al, referred to herein.

Enter:

/s/ Judge Abraham L. Marovitz

IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

NOS. 71-777 AND 71-807

No. 71-777

ROBERT E. CLEVELAND and
FRANCES H. CLEVELAND, etc.,
Petitioners,

v.

ILLINOIS BELL TELEPHONE COMPANY, an Illinois Corporation, and UNITED STATES OF AMERICA,
Respondents.

No. 71-807

ROBERT C. AGRON,
Petitioner,

v.

ILLINOIS BELL TELEPHONE COMPANY, et al.,
Respondents.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF RESPONDENT ILLINOIS BELL TELEPHONE COMPANY IN OPPOSITION

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

NOS. 71-777 AND 71-807

NO. 71-777

ROBERT E. CLEVELAND and
FRANCES H. CLEVELAND, etc.,
Petitioners,

v.

ILLINOIS BELL TELEPHONE COMPANY, an Illinois Corporation, and UNITED STATES OF AMERICA,
Respondents.

NO. 71-807

ROBERT C. AGRON,
Petitioner,

v.

ILLINOIS BELL TELEPHONE COMPANY, et al.,
Respondents.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF RESPONDENT ILLINOIS BELL TELEPHONE COMPANY IN OPPOSITION

Illinois Bell Telephone Company (Illinois Bell) opposes granting the writs of certiorari in Nos. 71-777 and 71-807 and for its reasons respectfully states:

STATUTES INVOLVED

In addition to the statutes referred to by petitioners, the following Illinois statutes and Internal Revenue Service rulings are involved: Section 8-11-2 of the Illinois Municipal Code (24 Ill. Rev. Stat. (1969) §8-11-2), Sections 467.1 and 467.2 of the Illinois Messages Tax (120 Ill. Rev. Stat. (1969) §§467.1-467.2), Section 36(a) and (b) of the Illinois Public Utilities Act (111⅔ Ill. Rev. Stat. (1969) §36(a), (b)), and Internal Revenue Service Rulings dated August 2, 1948, March 15, 1968, and March 31, 1969. These statutes and rulings are set out in the Appendix hereto.

STATEMENT

These petitions arise from a unanimous and well-reasoned decision of the United States Court of Appeals for the Seventh Circuit holding that the federal communications excise tax was "properly computed" (A. 5a)[1] and that the petitioners were not entitled to refunds. In No. 71-807, a challenge to the method of computing the federal tax was initiated by petitioner Robert C. Agron (Agron) who sought a refund of federal taxes allegedly overcollected from him by respondents. Agron's theory was that the federal tax on Illinois Bell's customers was overcollected to the extent that the base for taxation included amounts that customers paid under supplemental schedules filed by Illinois Bell with the Illinois Commerce Commission to recover the expenses of certain municipal occupation taxes and of part of the state Messages Tax imposed upon Illinois

[1] The Appendix to the *Agron* petition (No. 71-807) will be referred to herein as "A. . ." Illinois Bell's opposition to the *Cleveland* petition (No. 71-777) is treated separately beginning at p. 16, *infra*. Since the issues in *Agron* and *Cleveland* are essentially similar, much of the following statement is relevant to both cases. The Court of Appeals issued a single opinion.

Bell. The Court of Appeals, after considering the Illinois statutes and decisions involved, concluded that the state and local taxes are imposed upon Illinois Bell, not upon its customers (A. 6a-9a). Since Illinois Bell's charges to its customers to recover the expenses resulting from those taxes are made pursuant to schedules filed with the Illinois Commerce Commission (A. 13a), the Court of Appeals held that the computation and collection of "the tax imposed by section 4251 of the Internal Revenue Code does not result in any overassessment of the federal tax and . . . the district court erred in granting a tax refund to Agron" (A. 16a).

Having concluded that the federal tax was properly assessed, the Court of Appeals found it unnecessary to consider the other issues raised by Agron. These dealt with the district court's decision dismissing Counts II and III of Agron's complaint for want of jurisdiction. In Count II, Agron sought a refund from the United States on behalf of all Illinois Bell customers similarly situated on the basis of the same alleged overassessment. Illinois Bell was named as a party allegedly necessary for class relief. The district court held that Agron's "class action for tax refunds may not be maintained" because all members of the class did not file refund claims (A. 24a), that the "attempted joinder of a private litigant in a tax refund action is improper" (A. 25a) and that "since the relief to which plaintiff is entitled may occur without the involvement of IBT," Illinois Bell is "obviously not necessary in order to achieve a just adjudication" (*id.*). In Count III, Agron sought relief on behalf of members of the same class on the theory that they could file a derivative action on behalf of Illinois Bell against the United States. The district court denied the class relief and held that Illinois Bell "had no claim to press against the Government" since the federal tax "is imposed on telephone customers" not upon Illinois Bell (A. 25a) and since the obligation of Illinois Bell is "the collec-

tion and holding of certain tax revenues according to federal statutes, 26 U.S.C. §§4291, 7501(a) and policy" (A. 26a).

In challenging the propriety of the assessment and collection of the federal tax, Agron treats in a most summary and misleading fashion the terms of the federal statute and the Illinois statutes and court decisions relied upon by the Court of Appeals.

Under Illinois law, Illinois Bell is required to set forth all rates or charges for intrastate telephone service in schedules filed with the Illinois Commerce Commission (111⅔ Ill. Rev. Stat. (1969) §§ 36, 37). The schedules filed by Illinois Bell setting forth rates for telephone service are designed to recover all of the costs incurred by Illinois Bell in providing telephone service within Illinois, and a fair return on investment. *Illinois Bell Telephone Co.* v. *Illinois Commerce Commission,* 414 Ill. 275, 286, 111 N.E. 2d 329, 335 (1953).

It is an elementary principle of public utility rate regulation that taxes imposed upon a public utility are one of the expenses normally considered in determining the proper level of rates to be charged by that utility. As this Court has pointed out, "a proper allowance for taxes" is "normally included as a cost of service" in determining rates. *FPC* v. *United Gas Pipe Line Co.,* 386 U.S. 237, 243 (1967). Similarly, in Illinois Commerce Commission rate proceedings, various municipal, state and federal taxes imposed upon a telephone company are among the expenses included in determining the rates to be charged by that company. *E.g., Illinois Bell Telephone Company Proposed Advance in Rates,* 32 Ill. Comm. Comm'n. 149, 154-155 (1953). Since taxes imposed upon Illinois Bell are expenses for rate-making purposes just as are the costs of labor, materials and capital, the economic burden of all such taxes

is ultimately borne by Illinois Bell's customers through the rates charged for telephone service (A. 7a, 12a).

Among the various taxes imposed upon Illinois Bell which are recovered through the rates Illinois Bell charges its customers are municipal occupation taxes and the state Messages Tax. In 1955, Illinois enacted provisions authorizing municipalities to impose an occupation tax upon "persons engaged in the business of transmitting messages" (24 Ill. Rev. Stat. (1969) §8-11-2). The tax is not to exceed 5 percent of the gross utility receipts from business originating within the municipality imposing the tax (*id.*). At the present time, many Illinois municipalities, including Chicago, have elected to impose an occupation tax upon Illinois Bell (A. 2a). In 1965, Illinois increased the state Messages Tax, which is measured by a telephone company's gross receipts, from 3 percent to 4 percent, and in 1967, from 4 percent to 5 percent (120 Ill. Rev. Stat. (1969) § 467.1 *et seq.*). Like the municipal occupation taxes authorized by the state, the Act imposing this state gross receipts tax makes it clear that the "taxpayer" is a "person engaged in the business of transmitting messages" (120 Ill. Rev. Stat. (1969) §467.1). (A. 2a, 6a)[2]

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[2] The Illinois Department of Revenue has ruled that both the municipal occupation taxes and the state Messages Tax are imposed upon Illinois Bell and not upon its customers. The Department has stated that the municipal taxes are "occupation taxes whose legal incidence fall on . . . the person engaged in the business of transmitting messages. . . . They are not taxes which are levied on the customer . . ." (Bulletin accompanying March 14, 1956, amended Article 10 of Illinois Messages Tax Regulations). The Department has stated that the state Messages Tax "is imposed upon persons engaged in the business of transmitting messages in this State . . . and is not imposed upon persons for whom services within the Act are rendered by such taxpayers . . ." (Article 10b of Illinois Messages Tax Regulations).

Since these two gross receipts taxes imposed upon public utilities directly increase the costs of operation of the utilities, Illinois adopted a procedure to permit utilities expeditiously to recover the expenses resulting from the imposition upon them of these taxes. Instead of requiring Illinois Bell and other utilities to initiate a general rate proceeding to recover the additional expenses resulting from the enactment of the municipal taxes and the increase in the state Messages Tax above 3 percent, the Illinois statutes provide that utilities may file supplemental schedules to recover the expenses resulting from the imposition of these taxes and that such schedules may not be suspended pending Illinois Commerce Commission review (111⅔ Ill. Rev. Stat. (1969) § 36(a), (b)).

Paragraph (a) of Section 36 of the Illinois Public Utilities Act, which was added at the time municipalities were authorized to impose occupation taxes, applies "whenever a municipality pursuant to Section 8-11-2 [of the Municipal Code] . . . imposes a tax on any public utility. . . ." Under the procedures established in paragraph (a), a public utility "may charge its customers" to recover such municipal occupation tax expenses by filing "with the Commission a supplemental schedule applicable to such municipality which shall specify such additional charge." Paragraph (b) was added to Section 36 when Illinois raised the Messages Tax rate above 3 percent. Like paragraph (a), paragraph (b) permits a telephone company to recover the expense resulting from any increase above 3 percent in the Messages Tax by filing a supplemental schedule which sets forth an additional charge to its customers equal to the amount of the increase and such schedules may not be suspended pending Commission review (A. 3a, 4a).

In contrast to the municipal occupation taxes and the state Messages Tax which are imposed upon Illinois Bell,

the federal communications excise tax is imposed upon the customers of telephone companies. Section 4251 of the Internal Revenue Code provides that the excise tax "shall be paid by the person paying for the services" (26 U.S.C. § 4251(a)(1)). While the federal tax has been in effect, and until it is phased out pursuant to a recent act of Congress,[3] Illinois Bell is required to collect the federal excise tax which is imposed upon its customers, and in so doing, acts in a purely ministerial capacity pursuant to directions of the Internal Revenue Service (26 U.S.C. § 4291; see I.R.S. rulings in Appendix, *infra*). Illinois Bell is required to hold the federal taxes paid by and collected from its customers as "a special fund in trust for the United States" (26 U.S.C. § 7501(a)), and it pays over the amounts so collected each month to the Internal Revenue Service (26 C.F.R. § 49.6302(c)-1).

The federal tax applies to "all charges" paid by Illinois Bell customers for access to several types of service, including "local telephone service" and "toll telephone service" (26 U.S.C. § 4254(a)(1)). "Local telephone service" is defined in the Code as "the access to a local telephone system, and the privilege of telephonic quality communication. . . " (26 U.S.C. § 4252(a)(1)). The question of what a telephone customer must pay to obtain access to the telephone system is a matter of state law. As a public utility, Illinois Bell has a duty under Illinois law not to "charge, demand, collect or receive a greater or less or different compensation . . . for any service rendered or to be rendered, than the rates or other charges applicable to such . . . service as

[3] On December 31, 1970, Section 4251 was amended to provide for the complete elimination of the federal communications excise tax in a series of steps (P.L. 91-614). The rate of tax will remain 10% until January 1, 1973, at which time it will decrease 1% each year until January 1, 1982, after which the tax will not be imposed.

specified in its schedules on file and in effect at the time . . ." (111⅔ Ill. Rev. Stat. (1969) §§ 37, 39). Thus Illinois law provides that no Illinois Bell customer may have access to the telephone system unless he pays all charges pursuant to schedules filed by Illinois Bell with the Illinois Commerce Commission, including supplemental schedules filed with that Commission to recover the expenses of municipal occupation taxes and of part of the state Messages Tax imposed upon Illinois Bell. Since these municipal and state taxes imposed on Illinois Bell are expenses to be recovered through charges to its customers under schedules and supplemental schedules approved by the Illinois Commerce Commission, and since Illinois Bell customers must pay these charges to have access to the telephone system under the Illinois Public Utilities Act, the Court of Appeals has held that such charges are amounts paid for telephone service as defined in the Internal Revenue Code (26 U.S.C. §4252(a)(1)).[4]

THERE IS NO REASON FOR GRANTING THE WRIT IN NO. 71-807

1. The Court of Appeals unanimously and correctly concluded that the municipal occupation taxes and the state Messages Tax are imposed upon Illinois Bell, not upon its customers, and that charges to customers to recover ex-

[4] Illinois Bell had no discretion in including the amounts charged under supplemental schedules in the base upon which the federal communications excise tax is computed. This assessment was required by three directives of the Internal Revenue Service, dated August 2, 1948, March 15, 1968, and March 31, 1969, all of which are set forth in the Appendix hereto. Agron's assertion that "the IRS fashioned its special 1969 tax ruling for this case long after this litigation had begun in 1967" (Petition, p. 10), is simply untrue, since the 1969 ruling merely reaffirmed the principles set forth by the Internal Revenue Service in its ruling issued in 1948—over 20 years earlier.

penses incurred by Illinois Bell due to those taxes are charges for communications service (A. 12a). Thus, the court held these charges to be properly includable in the base upon which the federal communications excise tax is assessed. The court resolved the controlling question of state law—the nature of the charges made by Illinois Bell to recover the expenses of the state and local taxes imposed upon it—by applying relevant Illinois statutes and court rulings (A. 6a-9a).[5]

Agron's contention that "the court below never really considered" (Petition, p. 5) whether the charges of Illinois Bell to recover the expenses of the state and local taxes imposed upon it are charges for communications services within the federal statute cannot be reconciled with the Court of Appeals' decision, which considered and decided precisely that question (A. 12a, 13a-14a, 15a). After reviewing the "clear language of the Illinois statutes" and decisions of "the Illinois courts" showing that the state and local taxes are imposed upon Illinois Bell (A. 6a-7a), the Court of Appeals held that "amounts paid to reimburse IBT for its payment of the state and local messages taxes—just as amounts paid to reimburse IBT for all other taxes and for labor costs and equipment repairs—are paid for telephone service within the meaning of the [federal communications excise tax] statute" (A. 12a; see also A. 15a). Moreover, the court's holding that Illinois Bell's charges were properly includable in the federal tax base was unaffected by the separate statement of those charges by Illinois Bell on its customers' bills, since "neither IBT nor . . . Illinois can defeat that result by providing for the

[5] The Court of Appeals' decision is also completely consonant with subsequent decisions of the Illinois Supreme Court concerning the incidence and computation of taxes. See *Martin Oil Service, Inc.* v. *Department of Revenue*, 49 Ill. 2d 260, 273 N.E.2d 823 (1971).

itemization of those amounts passed on to customers which are attributable to taxes on IBT" (A. 14a).

There is no conflict between the decision of the Court of Appeals and any other decision construing the federal communications excise tax, the only federal statute at issue here. Further, the decision amply confirms a consistent series of Internal Revenue Service rulings dating back 20 years (see Appendix hereto). For these reasons, there is no merit whatever in Agron's attempt to have this Court review the judgment of the Court of Appeals.

2. In view of its dispositive holding that the computation and collection of "the tax imposed by section 4251 of the Internal Revenue Code does not result in any overassessment of the federal tax" (A. 16a), the Court of Appeals stated "we intimate no opinion on the correctness of the district court's dismissal of Counts II and III" (*id.*). However, the district court was clearly correct in holding that Agron's class action for a tax refund could not be maintained, that Illinois Bell could not be joined with the Government in a tax refund action and that Illinois Bell was not a necessary party to accord Agron any relief to which he might be entitled.

In an effort to invoke this Court's discretionary jurisdiction, Agron erroneously asserts that the question of whether a class action for a tax refund can be maintained, where, as here, each member of the purported class has not filed a claim for a refund, "has given difficulty to lower federal courts" (Petition, p. 13). Section 7422(a) of the Internal Revenue Code is unequivocal in its requirements concerning the filing of refund claims (26 U.S.C. §7422(a)):

> "No suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax . . . until a claim for a refund or credit has been duly filed with the Secretary . . . according to the provisions of law . . . and the regulations of the Secretary. . . ."

Moreover, every court which has considered this provision has ruled, as the district court did here, that a class action for a tax refund cannot be maintained on behalf of a purported class member who has not filed a properly documented refund claim.

The courts have uniformly held that each member of a class suing for a refund of federal taxes must have filed a proper claim for a refund in order for the suit to be maintained. For example, *Harkins* v. *United States,* 66-2 U.S.T.C. ¶9543 at 86,701 (E.D. Okla. 1966), *aff'd. on other grounds,* 375 F.2d 239 (10th Cir. 1967), involved a class action for a tax refund filed on behalf of the named plaintiffs, a husband and wife, "and for all those members of the Five Civilized Tribes similarly situated" to recover taxes on allegedly non-taxable income (*id.*, at 86,702). The plaintiff there contended that "all of the unnamed plaintiffs . . . and the amounts of refund due them are identifiable in the Internal Revenue Service files . . . and to require them to file individual claims for refund would be to unjustly enrich defendant at their expense . . ." (*id.*). The court granted the Government's motion to dismiss on the ground, among others, that "suit was filed without a proper claim for refund having been filed. The Treasury Regulations do not permit an unauthorized agent to claim an unspecified refund for unknown principals" (*id.*).

Similarly, in *McConnell* v. *United States,* 295 F. Supp. 605 (E.D. Tenn. 1969), the court refused to permit the named plaintiffs, a husband and wife, to maintain a tax refund action on behalf of the class of the striking employees of a company and their spouses. The members of the purported class had not filed claims for refunds. The court ruled that "before any taxpayer may maintain any action to recover any internal revenue tax . . . it is an absolute and indispensable prerequisite that such taxpayer shall have filed a claim for refund . . ." (*id.*, at 606).

This Court's decision in *United States* v. *Yellow Cab Co.*, 340 U.S. 543 (1951), lends no support to Agron's contention that "even if Rule 23 could be construed as an extension of the jurisdiction of the court [over tax refund actions]—which it is not—this authority was plainly granted by Congress in 28 U.S.C. §1346(a)(1)" (Petition, p. 17). *Yellow Cab* involved tort claims, jurisdiction over which is exclusively in the district courts under Section 1346(b). In contrast, the jurisdiction over actions seeking refunds of federal taxes is governed by Section 1346(a)(1) of the Judicial Code (28 U.S.C. §1346(a)(1)). That section establishes jurisdiction which is to be "concurrent with the Court of Claims" in "any civil action against the United States for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected" (*id.*).

In *United States* v. *Sherwood*, 312 U.S. 584 (1941), this Court considered the scope of concurrent jurisdiction such as that granted in Section 1346(a) to the district courts and the Court of Claims over certain actions, including those for a tax refund, brought against the United States.[6] Since the jurisdiction of the Court of Claims "is confined to the rendition of money judgments in suits brought for that relief against the United States," this Court concluded that "if the relief sought is against others than the United States the suit as to them must be ignored as beyond the jurisdiction of the court . . ." (*id.*, at 588).[7] Moreover, this Court

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[6] The action was brought pursuant to 28 U.S.C. §41(20). That section was reenacted in substantially identical form as 28 U.S.C. §1346(a)(2), which in turn confers concurrent jurisdiction in a form identical to that conferred by 28 U.S.C. §1346(a)(1).

[7] The Court in *Yellow Cab* noted that the scope of the jurisdiction granted by the Tort Claims Act is quite different from and "substantially broadens the jurisdiction of the District Courts as compared to that provided by the Tucker Act" which was involved in *Sherwood* (340 U.S. at 552).

specifically rejected an argument that the Rules of Civil Procedure expanded the limited and strictly defined jurisdiction of actions against the United States where the jurisdiction of the district court is concurrent with the Court of Claims (*id.*, at 591):

> "The matter is not one of procedure but of jurisdiction whose limits are marked by the Government's consent to be sued. That consent may be conditioned, as we think it has been here, on the restriction of the issues to be adjudicated in the suit, to those between the claimant and the Government. The jurisdiction thus limited is unaffected by the Rules of Civil Procedure, which prescribe the methods by which the jurisdiction of the federal courts is to be exercised but do not enlarge the jurisdiction."

In these circumstances, it is clear that the district court correctly held that Rule 23 does not avoid the jurisdictional prerequisite to maintaining a tax refund action that each individual seeking such a refund must have filed a claim for a refund before instituting suit. Agron's contention that this prerequisite is unnecessary "where, as here, there is involved only an issue of law and there is nothing of an administrative nature to be done" (Petition, p. 18) is plainly incorrect. As the court pointed out in *Eisen* v. *Carlisle & Jacquelin*, 391 F.2d 555, 567 (2d Cir. 1968), judicial intervention is only appropriate in situations where there is "no public administrative body that could ensure repayment, so the responsibility must ultimately rest on the judicial system." However, here the Internal Revenue Code has established a procedure for passing upon claims for refunds of federal taxes and bypass judicial intervention in

the absence of filing such claims is both unnecessary and inappropriate.[8]

3. Agron asserts that he "does not argue . . . but reserves" (Petition, p. 3) the issues respecting the district court's rulings that the "attempted joinder of a private litigant [Illinois Bell] in a tax refund action is improper" and that the joinder of Illinois Bell "is obviously not necessary . . . to achieve a just adjudication" (A. 25a). Even if this Court were to consider whether to review these issues, such review would not be warranted because the district court's decision dismissing Illinois Bell as a party was plainly correct. This Court's decision in *United States* v. *Sherwood, supra,* establishes that the joinder of a private litigant with the United States in actions for the recovery of money from the United States is improper where, as in tax refund actions, there is concurrent jurisdiction between the district courts and the Court of Claims.[9]

In asserting that Illinois Bell's joinder "was necessary and proper" (Petition, p. 3), Agron sets forth a series of assertions concerning Illinois Bell's record keeping and retention procedures which have no support whatever in the record. Basically, Agron argues that Illinois Bell is a necessary party because "administratively a refund will be

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[8] Agron's reliance upon *Oatis* v. *Crown Zellerbach Corp.*, 398 F. 2d 496 (5th Cir. 1968), to support his contention that "the exhaustion doctrine has been satisfied" (Petition, p. 18) is misplaced. That case involved discriminatory employment practices and a complaint brought under Title VII of the Civil Rights Act, establishing an administrative agency which can only endeavor to effect voluntary conciliations and has no power to award damages or to grant injunctive relief (42 U.S.C. §2000(e) *et seq.*).

[9] The rule enunciated in *Sherwood* has been followed in tax refund actions and required that Illinois Bell be dismissed as a defendant in the district court. See, *e.g., De Van* v. *United States,* 50 F. Supp. 992 (D.N.J. 1943).

most feasible if carried out through IBT" (*id.*, at 4). As is shown in the detailed affidavit of Mr. R. H. Phelps submitted by Illinois Bell in the district court, however, Illinois Bell does not maintain records of the amounts that would be due under Agron's theory from the United States as a refund to each Illinois Bell customer. That affidavit also shows that although Illinois Bell does maintain records from which the amounts of disputed federal tax could be approximately calculated by subscriber for the most recent six-month period, the cost to Illinois Bell of such an undertaking would far exceed the gross amount of the disputed federal tax for that period (Phelps Aff., pp. 61-62[10]). And for any period beyond the most recent six months, Illinois Bell only retains summary records which would be of no use whatever in the determination of individual refunds (*id.*, at 53-56).

Agron has never offered any evidence disputing these facts. Moreover, there is no showing that other Illinois Bell customers cannot pursue the administrative machinery established by the Internal Revenue Service for passing upon refund claims. Contrary to Agron's assertion, those of Illinois Bell's customers who are interested in claiming a refund are, like Agron, in a better position than Illinois Bell to determine the amount of such a refund. Thus, there is no basis for abandoning the established administrative refund machinery of the Internal Revenue Service and substituting in its place an extra-statutory refund process supervised by the judiciary. The district court's decision that there is no basis for involving Illinois Bell in this dispute between Agron and the Government would not warrant review even if this Court were to decide to review the Court of Appeals'

[10] Page references to Mr. Phelps' affidavit are to the Joint Appendix in the Court of Appeals.

decision on the propriety of the assessment of the federal communications excise tax.[11]

THERE IS NO REASON FOR GRANTING THE WRIT IN NO. 71-777

The Court of Appeals correctly affirmed the district court's decision dismissing the complaint of Robert E. and Frances H. Cleveland (Cleveland) (No. 71-777). Like the complaint in *Agron*, Cleveland erroneously alleged "that state and municipal taxes are not proper charges to be included in determining the federal tax base . . . thereby entitling plaintiffs to a refund" (A. 25a).[12] However, Cleveland did not file any claim for a refund with the Internal Revenue Service.

Cleveland's action was originally commenced against Illinois Bell alone in October, 1969, in the Circuit Court of Cook County, Illinois. Since Cleveland's state court complaint questioned the proper method of assessing the fed-

[11] The district court correctly dismissed Count III of Agron's complaint, which was "in the nature of a class derivative action brought on behalf of IBT, plaintiff's theory being that IBT breached its fiduciary duty to the class to prevent its subscribers from being overcharged" (A. 25a). The same jurisdictional defects in Count II—improperly seeking to bring a class action for a tax refund and improper joinder—also required dismissal of Count III (*id.*). Moreover, since the federal tax is not imposed upon Illinois Bell and its role in the collection and assessment of that tax is purely ministerial, Illinois Bell "had no claim to press against the Government" (*id.*). Finally, consideration of Count III is barred by the doctrine of *res judicata*, since the same issue involved in Count III was unsuccessfully litigated by petitioner in a prior case—*Agron* v. *Illinois Bell Telephone Co., et al.* (No. 67 C 2041, N.D. Ill. Aug. 4, 1969).

[12] This reference to the Appendix and all others in the remainder of the brief are to the Appendix to the *Cleveland* petition and will be referred to as "A. . ."

eral communications excise tax and sought a refund of amounts allegedly improperly collected, Illinois Bell filed a timely petition, pursuant to 28 U.S.C. §1441, to remove the action to the United States District Court. The district court denied Cleveland's motion to remand (A. 24a-27a) and subsequently dismissed Cleveland's complaint on motion of Illinois Bell and the United States (A. 27a-29a).

The Court of Appeals held that since "IBT properly computed the federal tax in accordance with the provisions of the Internal Revenue Code, the underlying basis of the Clevelands' complaint falls" (A. 15a). While the Court of Appeals did not pass upon the other issues raised by Cleveland, the district court had properly dismissed Cleveland's complaint for failure to file any claim for a refund before instituting his action. No basis has been advanced in his petition for reviewing that judgment.

Despite the requirement of Section 7422(a) that "no suit . . . shall be maintained in any court for the recovery of any internal revenue tax . . . until a claim for a refund . . . has been duly filed . . ." (26 U.S.C. §7422(a)), Cleveland by his own admission failed to file any claim for a refund before instituting this action. In *United States* v. *Felt & Tarrant Manufacturing Co.*, 283 U.S. 269, 272-273 (1931), this Court held that "the filing of a claim . . . as a prerequisite to a suit to recover taxes paid is a familiar provision of the revenue laws, compliance with which may be insisted upon . . ." and also emphasized that "the necessity for filing a claim such as the statute requires is not dispensed with because the claim may be rejected."

Similarly, Cleveland advances no basis for reviewing the district court's judgment denying his motion to remand this action to the state court. As the district court pointed out, "to say that this action is not brought for a refund of taxes or that the United States is not charging the tax is absurd

because, as the complaint alleged, the money was assessed pursuant to federal law regarding communication taxes, 28 U.S.C. §§ 4251-54" (A. 27a).

CONCLUSION

For the foregoing reasons, the petitions for writs of certiorari to the United States Court of Appeals for the Seventh Circuit in *Agron* (No. 71-807) and *Cleveland* (No. 71-777) should be denied.

Respectfully submitted,

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Chicago, Illinois 60670
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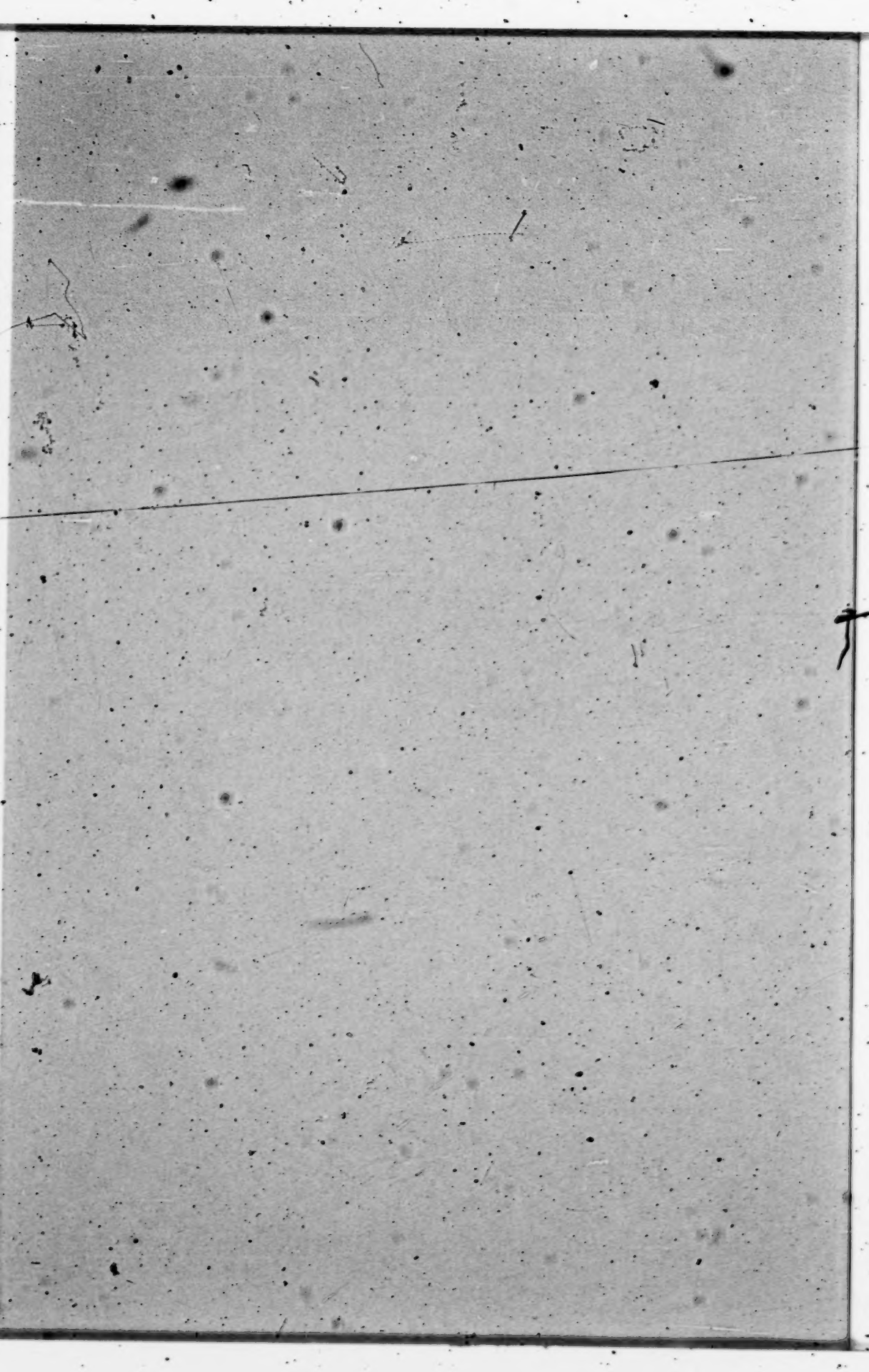
Of Counsel:
SIDLEY & AUSTIN

January 31, 1972



24 Ill. Rev. Stat. (1969) §8-11-2:

§8-11-2. *Taxation of occupations or privileges*

The corporate authorities of any municipality may tax any or all of the following occupations or privileges:

1. Persons engaged in the business of transmitting messages by means of electricity, at a rate not to exceed 5% of the gross receipts from such business originating within the corporate limits of the municipality.

2. Persons engaged in the business of distributing, supplying, furnishing, or selling gas for use or consumption within the corporate limits of the municipality, and not for resale, at a rate not to exceed 5% of the gross receipts therefrom.

3. Persons engaged in the business of distributing, supplying, furnishing, or selling electricity for use or consumption within the corporate limits of the municipality, and not for resale, at a rate not to exceed 5% of the gross receipts therefrom.

4. Persons engaged in the business of distributing, supplying, furnishing, or selling water for use or consumption within the corporate limits of the municipality, and not for resale, at a rate not to exceed 5% of the gross receipts therefrom.

None of the taxes authorized by this Section may be imposed with respect to any transaction in interstate commerce or otherwise to the extent to which such business may not, under the constitution and statutes of the United States, be made the subject of taxation by this State or any political sub-division thereof; nor shall any persons engaged in the business of distributing, supplying, furnishing or selling gas, water or electricity, or engaged in the business of transmitting messages be subject to taxation under the provisions of this section for such transactions as are or may become subject to taxation under the provisions of

the "Municipal Retailers' Occupation Tax Act" authorized by Section 8-11-1; nor shall any tax authorized by this section be imposed upon any person engaged in a business unless such tax is imposed in like manner and at the same rate upon all persons engaged in businesses of the same class in the municipality, whether privately or municipally owned or operated.

Any of the taxes enumerated in this section may be in addition to the payment of money, or value of products or services furnished to the municipality by the taxpayer as compensation for the use of its streets, alleys, or other public places, or installation and maintenance therein, thereon or thereunder of poles, wires, pipes or other equipment used in the operation of the taxpayer's business.

For the purpose of the taxes enumerated in this section:

"Gross receipts" means the consideration received for the transmission of messages, the consideration received for distributing, supplying, furnishing or selling gas for use or consumption and not for resale, and the consideration received for distributing, supplying, furnishing or selling electricity for use or consumption and not for resale, and the consideration received for distributing, supplying, furnishing or selling water for use or consumption and not for resale, and for all services rendered in connection therewith valued in money, whether received in money or otherwise, including cash, credit, services and property of every kind and material and for all services rendered therewith, and shall be determined without any deduction on account of the cost of transmitting such messages, without any deduction on account of the cost of the service, product or commodity supplied, the cost of materials used, labor or service cost, or any other expenses whatsoever.

The words "transmitting messages", in addition to the usual and popular meaning of person to person communication, shall include the furnishing, for a consideration, of

services or facilities (whether owned or leased), or both, to persons in connection with the transmission of messages where such persons do not, in turn, receive any consideration in connection therewith, but shall not include such furnishing of services or facilities to persons for the transmission of messages to the extent that any such services or facilities for the transmission of messages are furnished for a consideration, by such persons to other persons, for the transmission of messages.

"Person" as used in this section means any natural individual, firm, trust, estate, partnership, association, joint stock company, joint adventure, corporation, municipal corporation or political subdivision of this State, or a receiver, trustee, conservator or other representative appointed by order of any court.

Illinois Messages Tax Act, 120 Ill. Rev. Stat. (1969) §§467.1-467.2:

§467.1 *Definitions*

For the purposes of this Act:

"Gross receipts" means the consideration received for the transmission of messages and for all services rendered in connection therewith, valued in money, whether received in money or otherwise, including cash, credits, services and property of every kind or nature, and shall be determined without any deduction on account of the cost of transmitting such messages, the cost of materials used, labor or service costs or any other expense whatsoever. However, any charges added to customers' bills pursuant to the provisions of paragraph (b) of Section 36 of "An Act concerning public utilities", approved June 29, 1921, as amended, or any charges added to customers' bills by taxpayers who are not subject to rate regulation by the Illinois Commerce Commission because of the tax that is imposed by this Act on any such taxpayer, shall be excluded in determining such

gross receipts. In case credit is extended, the amount thereof shall be included only as and when payments are received.

The words, "transmitting messages," in addition to the usual and popular meaning, include the furnishing, for a consideration, of services or facilities (whether owned or leased), or both, to persons in connection with the transmission of messages where such persons do not, in turn, receive any consideration in connection therewith, but do not include such furnishing of services or facilities to persons for the transmission of messages to the extent that any such services or facilities for the transmission of messages are furnished for a consideration, by such persons to other persons, for the transmission of messages.

"Department" means the Department of Revenue of the State of Illinois.

"Director" means the Director of Revenue for the Department of Revenue of the State of Illinois.

"Taxpayer" means a person engaged in the business of transmitting messages.

"Person" means any natural individual, firm, trust, estate, partnership, association, joint stock company, joint adventure, corporation, or a receiver, trustee, conservator or other representative appointed by order of any court, or any city, town, county or other political subdivision of this State.

§467.2 *Rate of tax—Interstate business exempt*

A tax is imposed upon persons engaged in the business of transmitting messages in this State at the rate of 5% of the gross receipts from such business, provided that any change in rate imposed by this amendatory Act of 1967 shall become effective only with bills having a date on or after August 1, 1967. However, such tax is not imposed

upon the privilege of engaging in any business in interstate commerce or otherwise to the extent to which such business may not, under the Constitution and statutes of the United States, be made the subject of taxation by this State.

111-2/3 Ill. Rev. Stat. (1969) §§36, 36(a), 36(b):

§36. *Change of rates—Notice—Suspension of rates—Temporary schedule—Charge for taxes*

* * * *

(a) Whenever a municipality pursuant to Section 8-11-2 of the Illinois Municipal Code, as heretofore and hereafter amended, imposes a tax on any public utility, such utility may charge its customers, in addition to any rate authorized by this Act, an additional charge equal to the sum of (1) an amount equal to such municipal tax, or any part thereof, (2) 3% of such tax, or any part thereof, as the case may be, to cover costs of accounting, and (3) an amount equal to the increase in taxes and other payments to governmental bodies resulting from the amount of such additional charge. Such utility shall file with the Commission a true and correct copy of the municipal ordinance imposing such tax; and also shall file with the Commission a supplemental schedule applicable to such municipality which shall specify such additional charge and which shall become effective upon filing without further notice. Such additional charge shall be made by the addition of a uniform percentage to the amounts payable for intrastate utility service in such municipality and shall be shown separately on the utility bill to each customer. The Commission shall have power to investigate whether or not such supplemental schedule correctly specifies such additional charge, but shall have no power to suspend such supplemental schedule. If the Commission finds, after a hearing, that such supplemental schedule does not correctly specify such additional charge, it shall by order require a refund to the appropriate customers of the excess, if any, with interest, in such man-

ner as it shall deem just and reasonable, and in and by such order shall require the utility to file an amended supplemental schedule corresponding to the finding and order of the Commission.

(b) Whenever the tax that is imposed upon a public utility engaged in the business of transmitting messages pursuant to Section 2 of The Messages Tax Act, or whenever the tax that is imposed upon a public utility engaged in the business of distributing, supplying, furnishing or selling gas for use or consumption pursuant to Section 2 of The Gas Revenue Tax Act, or whenever the tax that is imposed upon a public utility engaged in the business of distributing, supplying, furnishing or selling electricity for use or consumption pursuant to Section 2 of The Public Utilities Revenue Act, shall exceed the rate of 3% of the gross receipts, as defined in said Acts, respectively, from any such business, such utility may charge its customers, in addition to any rate authorized by this Act, an additional charge equal to the amount by which such tax exceeds 3%. Such utility shall file with the Commission a supplemental schedule which shall specify such additional charge and which shall become effective upon filing without further notice. Such additional charge shall be made by the addition of a uniform percentage to the amounts payable for intrastate utility service. The Commission shall have the power to investigate whether or not such supplemental schedule correctly specifies such additional charge, but shall have no power to suspend such supplemental schedule. If the Commission finds, after a hearing, that such supplemental schedule does not correctly specify such additional charge, it shall by order require a refund to the appropriate customers of the excess, if any, with interest, in such manner as it shall deem just and reasonable, and in and by such order shall require the utility to file an amended supplemental schedule corresponding to the finding and order of the Commission.

Internal Revenue Service Rulings

TREASURY DEPARTMENT.
Washington 25.

Aug. 2, 1948

American Telephone and Telegraph Company
195 Broadway
New York 7, New York

Attention: Mr. Martin J. Karl

Gentlemen:

Reference is made to your letter of December 10, 1947, submitting on behalf of the Pacific Telephone and Telegraph Company and its exchange service customers in various municipalities in the State of Washington the following questions for Bureau rulings:

> "(1) Whether amounts billed to customers of telephone service in municipalities in the State of Washington which represent taxes paid to such municipalities by the company and which, pursuant to an order of the Department, are passed on to the customers on a pro rata basis; constitute amounts paid for telephone services and facilities subject to the taxes imposed by section 3465 of the Internal Revenue Code?
>
> "(2) Whether such amounts are deductible by customers for income tax purposes under section 23(c)(3) of the Internal Revenue Code and Sec. 29.23(c)-1(b) of Regulations 111 where they are paid otherwise than in connection with the customers' trade or business?"

It is stated that the above questions arise by reason of an order issued on October 9, 1947, by the Department of Public Utilities of Washington authorizing the Pacific Telephone and Telegraph Company to bill on a pro rata

basis, to its customers in various municipalities in Washington, municipal occupation, business, excise and use of streets taxes imposed by such municipalities under the provisions of municipal ordinances.

Your letter enclosed copies of ordinances of the cities of Seattle, Spokane and Tacoma, relating to, and providing for, a license fee or tax upon certain businesses, occupations, pursuits and privileges, a copy of the Department's order describing the history of proceedings before the Department, the Superior Court of Thurston County in Washington, and the Supreme Court of the State of Washington prior to the order and setting forth the Department's findings and orders, and a photostatic copy of the portion of the Supreme Court's decision which relates to the passing on to customers, of payments to municipalities.

The evidence discloses that the taxes are levied upon the telephone company and represent payments which the company is required to make to the various municipalities in connection with its operations therein. Some of the taxes are based on gross receipts while others are specified annual and daily amounts. The taxes are universally considered proper items of operation expense, to be so considered by State rate-making authorities. The Department has the power to fix the special exchange rate applicable to the different municipalities, which will in effect require the rate payers in each municipality to absorb on a pro rata basis a sum equal to the amount of the tax the telephone company is required to pay such municipality.

Answering question No. (1), inasmuch as the payments which the telephone company must make to the various municipalities in connection with its operations therein, are considered proper items of operation expense, it is held that the pro rata shares of such payments the ratepayers are required to absorb, which are billed by the company

to its customers, constitute charges for telephone services and facilities subject to the tax imposed by section 3465 of the Code, as amended.

The answer to question No. (2) will be made the subject of a separate communication.

Very truly yours,

/s/

Commissioner.

U. S. TREASURY DEPARTMENT
Office of Chief Counsel, Internal Revenue Service,
Washington, D. C. 23224.

Date March 15, 1968

In reply refer to:
CC:CL-3767/O:RJS

Mr. Victor E. Ferrall
General Tax Attorney
American Telephone and
Telegraph Company
195 Broadway
New York, N. Y. 10007

Re: Agron v. Illinois Bell Telephone Co.

and

American Telephone and Telegraph Company
U. S. D. C. Illinois, # 67C-2041
Your ref: C

Dear Mr. Ferrall:

This refers to your December 12, 1967 letter addressed to the Commissioner, the receipt of which has heretofore been acknowledged by this office. Attached to your cor-

respondence was a copy of a complaint filed recently in the United States District Court for Illinois against Illinois Bell Telephone Company, wherein the plaintiff, a subscriber, seeks a declaratory judgment respecting the determination of the Federal Communication Excise Tax charged and collected by that company. Also attached was a copy of a letter ruling dated August 2, 1948, which this Agency issued to American Telephone and Telegraph Company.

In response to your inquiry, you are advised that the current position of the Internal Revenue Service regarding the tax imposed by section 4251 of the Internal Revenue Code of 1954, is still represented by the aforementioned ruling, namely, that the payments which the telephone company must make to various municipalities in connection with its operations therein, are considered proper items of operation expense and therefore the pro rata shares of such payments billed by the company, which the ratepayers are required to absorb, constitute charges for telephone service subject to the Federal tax on communication services and facilities.

No decision has yet been reached with respect to the question of participation by the United States in the instant lawsuit. In this connection we acknowledge receipt of your letter of February 1, 1968, with which you forwarded a copy of the answer and third-party complaint filed in the above-entitled case. The matter is under consideration and we will let you know when any determination has been made with respect thereto.

Very truly yours,

/s/ Lester R. Uretz,
Lester R. Uretz,
Chief Counsel.

REV. RUL. 69-151,
1969-13 INTERNAL REVENUE BULLETIN 16
(March 31, 1969)

Advice has been requested whether certain amounts separately stated on customers' bills from telephone companies may be excluded in determining the amount upon which the Federal communications tax is imposed by Section 4251(a)(1) of the Internal Revenue Code of 1954. These amounts are attributable to State and local taxes (variously categorized as "gross receipts," "occupational," "message," etc., taxes) imposed on the telephone companies but passed on to the customers as separate charges.

Section 4251(a)(1) of the Code imposes a tax on certain communications services, including local telephone service. That section provides that this tax shall be paid by the person paying for the services.

Section 4252(a) of the Code provides that for purposes of the Federal communications tax the term 'local telephone service' means (1) the access to a local telephone system and the privilege of telephonic quality communication with substantially all persons having telephone or radio telephone stations constituting a part of such local telephone system, and (2) any facility or service provided in connection with a service described in (1).

Section 4254(a)(1) of the Code provides, with an exception not here material, that the amount on which the tax with respect to such services shall be based shall be the sum of all charges for such services included in the bill.

Unlike the Federal communications tax, which is imposed on the person paying for the service, the State and local taxes under consideration are imposed on the companies engaged in the business of providing the service. Since these taxes are directly attributable to the telephone

services provided, they constitute an element of the cost of providing the services along with the costs attributable to labor and equipment. The fact that amounts attributable to such taxes are passed on and are separately stated on bills sent to customers does not change the legal incidence of the taxes. Therefore, the practical effect of separately stating amounts attributable to State and local taxes on bills sent to customers is simply to identify an element of the total charges for the telephone services provided to such customers.

Accordingly, it is held that amounts attributable to the State and local taxes referred to above, which are imposed on telephone companies but are passed on to customers and separately stated on customers' bills, may not be excluded in determining the amount upon which the Federal communications tax is imposed by section 4251(a)(1) of the Code.

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Nos. 71-777 and 71-807

In the Supreme Court of the United States

OCTOBER TERM, 1971

ROBERT E. CLEVELAND AND FRANCES H. CLEVELAND, PETITIONERS

v.

ILLINOIS BELL TELEPHONE COMPANY, AN ILLINOIS CORPORATION, AND UNITED STATES OF AMERICA

ROBERT C. AGRON, PETITIONER

v.

ILLINOIS BELL TELEPHONE COMPANY AND UNITED STATES OF AMERICA

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

ERWIN N. GRISWOLD,
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SCOTT P. CRAMPTON,
Assistant Attorney General,
GILBERT E. ANDREWS,
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Department of Justice,
Washington, D.C. 20530.

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In the Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-777

ROBERT E. CLEVELAND AND FRANCES H. CLEVELAND, PETITIONERS

v.

ILLINOIS BELL TELEPHONE COMPANY, AN ILLINOIS CORPORATION, AND UNITED STATES OF AMERICA

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ILLINOIS BELL TELEPHONE COMPANY AND UNITED STATES OF AMERICA

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion and order of the district court in No. 71-777 (Pet. App. 24a-29a) are unreported. The two opinions of the district court in No. 71-807 (Pet. App. 18a-26a) are reported at 319 F. Supp. 418 and 325 F.

Supp. 487. The opinion of the court of appeals in both cases (No. 71–777, Pet. App. 1a–15a; No. 71–807, Pet. App. 1a–17a) is reported at 449 F. 2d 906.

JURISDICTION

The judgments of the court of appeals were entered on September 22, 1971. The petitions for writs of certiorari were filed on December 11, 1971, in No. 71–777, and on December 18, 1971, in No. 71–807. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether petitioners may exclude from the base upon which the 10 percent federal tax on "amounts paid for * * * communication services", imposed by Section 4251 of the Internal Revenue Code of 1954, is computed, any part of the telephone rates authorized by Illinois law and charged and collected by Illinois Bell Telephone Company because those rates reflected operating costs including, among other items, increased state and municipal taxes imposed upon and collected from the telephone company.

2. Whether petitioners may maintain class actions for refunds of unstated amounts of federal taxes to unnamed and unidentified taxpayers who have not filed the claims for refund required by Section 7422(a) of the Internal Revenue Code as a prerequisite to the maintenance of a suit for the recovery of any internal revenue tax.

STATUTES INVOLVED

Sections 4251(a), 4252 (a) and (b), and 4254 (a) and (b) of the Internal Revenue Code of 1954 are set forth

in the Appendix to the petition in No. 71–807 (pp. 27a–28a). Pertinent sections of the Illinois statutes are set forth in the Appendix to the brief in opposition of respondent Illinois Bell Telephone Company (pp. A1–A6). Sections 6402(a) and 7422(a) of the Internal Revenue Code of 1954 are set forth in the Appendix, *infra*, p. 13.

STATEMENT

Petitioners are residents of Chicago, Illinois, and are subscribers to telephone services supplied there by Illinois Bell Telephone Company ("Illinois Bell"), a public utility whose intrastate rates are regulated by Illinois law and the Illinois Commerce Commission. As telephone subscribers, petitioners are and have been subject to the tax at the rate of 10 percent imposed on "amounts paid for * * * communication services" by Section 4251 of the Internal Revenue Code. As provided therein, the tax is to be "paid by the person paying for the services"; but, as required by Section 4291, it is collected by Illinois Bell, and remitted to the United States.

For over thirty years, the State of Illinois has imposed upon persons engaged in various businesses, including public utilities, a number of "occupation taxes." One of these has been a tax "upon persons engaged in the business of transmitting messages," measured by "gross receipts from such business." Smith-Hurd Ill. Ann. Stat., c. 120, §§ 467.1, 467.2. In 1955,[1] the State authorized municipalities to tax (at rates not to exceed 5 percent of gross receipts

[1] 1955 Laws of Illinois, p. 1900. Approved July 14, 1955.

from intrastate service in the taxing municipality) the occupations of various public utilities, including that of "[p]ersons engaged in the business of transmitting messages by means of electricity * * *." Smith-Hurd Ill. Ann. Stat., c. 24, § 8–11–2. Since that time, over seventy Illinois municipalities, including the City of Chicago, have imposed occupation taxes at rates up to 5 percent upon Illinois Bell. At the same session, the Legislature, by statute approved the same day,[2] amended the basic utility regulatory statute (Smith-Hurd Ill. Ann. Stat., c. 111 2/3) by adding what is now § 36(a), authorizing a utility subjected to the municipal occupation taxes to charge its customers for intrastate service in the taxing municipality, in addition to any rate otherwise authorized, an additional charge equal to (1) the amount of the municipal tax, or any part thereof, (2) 3 percent thereof to cover accounting costs, and (3) an amount equal to the increase in taxes and other payments to governmental bodies resulting from the additional charge. Such an increase in rates was to be made as others were—by filing a supplemental schedule specifying the additional charge with the Illinois Commerce Commission. The additional charge was to be shown separately on the utility bill to customers. The Commerce Commission could investigate to determine whether the additional charge was within the statutory formula, and could order refunds if it was excessive, but otherwise could not suspend this statutorily authorized increase, as it could with other revised rate schedules proposing increases.

[2] 1955 Laws of Illinois, p. 3022. Approved July 14, 1955.

When municipalities have imposed the occupation tax measured by gross receipts from service within the municipality, Illinois Bell has usually filed supplemental schedules of rates pursuant to the authority of § 36(a) and has billed its customers within the municipality accordingly.

In 1965, the Legislature of Illinois increased the rate of the state occupation tax upon "persons engaged in the business of transmitting messages" from 3 percent to 4 percent [3] (and in 1967 to 5 percent), and at the same time further amended the utility regulatory statute by adding § 36(b),[4] which performed substantially the same function in authorizing an additional charge with respect to the increase in the rate of the state tax that § 36(a) had performed with respect to newly imposed municipal occupation taxes. Illinois Bell has paid the state tax at the increased rates, has filed with the Commerce Commission appropriate supplemental schedules, and has made and collected the additional charge authorized. Section 36(b) did not require that the additional charge authorized thereunder be separately indicated on bills to customers, as § 36(a) did. It appears, however, that Illinois Bell has shown the additional charge separately on bills.

Illinois Bell, in accordance with rulings issued by the Commissioner of Internal Revenue, has collected and remitted to the United States the federal tax imposed by Section 4251 of the Internal Revenue Code

[3] 1965 Laws of Illinois, p. 1684. Approved July 16, 1965.
[4] 1965 Laws of Illinois, p. 1679. Approved July 16, 1965.

upon "amounts paid for * * * communication services" by computing it upon "the sum of all charges for such services included in the bill," as required by Section 4254, including the additional charges authorized by § 36 (a) and (b) of the Illinois statute.

Petitioner Agron filed a claim for refund of the communication tax in the amount of $23.98, asserting that, for a period beginning in 1965 and through the first three quarters of 1968, the tax he had paid had been improperly computed by virtue of including in its base the additional charges billed by Illinois Bell. At the same time, petitioner Agron filed a purported claim for refund of communication tax in an unstated amount, allegedly on behalf of unspecified and unnamed taxpayers ("all other telephone subscribers of Illinois Bell Telephone Company who are situated similarly to him"). Both claims were denied, and suit on three counts against the United States and Illinois Bell was thereafter instituted, asserting: in Count I, a claim for $23.98 on behalf of petitioner individually; in Count II, a class action on behalf of unnamed taxpayers who had not filed claims for refund; and, in Count III, a purported derivative action seeking refund to Illinois Bell of taxes collected by it from its customers, and by it paid over to the United States. Illinois Bell was thereafter voluntarily dismissed as a defendant under Count I by petitioner. On cross motions for summary judgment, the district court entered judgment for petitioner for $23.98 under Count I, but dismissed Counts II and III. On cross appeals, the court of appeals

reversed the judgment for petitioner on Count I, and dismissed petitioner's appeals on Counts II and III.

In No. 71-777, without having filed any claim for refund, the petitioners Cleveland instituted a similar individual and class suit against Illinois Bell alone in a state court in Illinois, demanding also declaratory and injunctive relief. The suit was removed to the United States District Court by Illinois Bell, and peitioners' motion to remand was denied. The United States was thereafter added as a defendant. On motions of the defendants, the suit was dismissed by the district court, and its order was affirmed by the court of appeals.

ARGUMENT

The decisions below are correct. There is no conflict of decisions or any other basis for review by this Court.

1. Petitioners contest the increase in the federal tax on amounts paid for communication services resulting from an increase in telephone rates authorized by Illinois law. Since the federal tax is 10 percent of the sum of all charges for such services, an increase in telephone rates inevitably results in an increase in the federal tax. Petitioners' claim is therefore groundless. It is no more significant that the rate increase was occasioned by an increase in municipal and state taxes imposed upon the telephone company than it would have been if the rate increase had been occasioned by increased costs of labor or materials. This Court has recognized that taxes imposed upon utilities are costs that must be included in the utilities'

rate structures and recovered by charges to their customers. *Federal Power Commission* v. *United Gas Pipe Line Co.*, 386 U.S. 237, 243; *Georgia Railway & Power Co.* v. *Railroad Commission*, 262 U.S. 625, 632–633; *Galveston Electric Co.* v. *Galveston*, 258 U.S. 388, 399.

In an effort to avoid the inevitable conclusion that the federal tax was properly increased as the telephone company's rates increased, petitioners assert that the Illinois municipal and state occupation taxes upon the telephone company were in fact taxes upon the customers of the telephone company, and for that reason improperly included in the base of the federal tax. This, of course, is entirely a matter of Illinois law, and hardly calls for review by this Court. In any event, the same argument has in a number of contexts been rejected by the Supreme Court of Illinois both as a matter of statutory construction and as a matter of constitutional imperative under the Illinois constitution. *Reif* v. *Barrett*, 355 Ill. 104, 188 N.E. 889; *People's Drug Shop, Inc.* v. *Moysey*, 384 Ill. 283, 51 N.E. 2d 144; *Vause & Striegel, Inc.* v. *McKibbin*, 379 Ill. 169, 39 N.E. 2d 1006; *International Business Machines Corp.* v. *Department of Revenue*, 25 Ill. 2d 503, 185 N.E. 2d 257. And this Court similarly has held that the parallel Illinois occupation tax upon retailers, measured by gross receipts from sales to the United States, was not a tax upon the United States. *United States* v. *Department of Revenue*, 371 U.S. 21, affirming 202 F. Supp. 757 (N.D. Ill.).

Petitioners also stress that the additional charge (which was not the amount of the municipal and state

taxes, but a composite of factors) was separately stated on the telephone company's bills. But both the Illinois Supreme Court and this Court have held that the separate statement of a tax is of no significance in determining its incidence. See *Fischman & Sons, Inc.* v. *Department of Revenue*, 12 Ill. 2d 253, 146 N.E. 2d 54; *Alabama* v. *King & Boozer*, 314 U.S. 1; cf. *Wilmette Park Dist.* v. *Campbell*, 338 U.S. 411, 418. This Court, moreover, pointed out in *Lash's Products Co.* v. *United States*, 278 U. S. 175, 176, that:

> The phrase "passed the tax on" is inaccurate, as obviously the tax is laid and remains on the manufacturer * * *. The purchaser does not pay the tax. He pays or may pay the seller more for the goods because of the seller's obligation, but that is all. * * *

These observations constitute an effective answer to petitioners' claim that Illinois law, as they read it, reduces the base upon which the federal tax should be computed.[5] The economic impact of a tax upon a pro-

[5] Petitioners' arguments present but slight, if any, verbal variants upon arguments that have frequently and unsuccessfully, been advanced in state courts where the base upon which a sales or gross receipts tax is computed has been enlarged because an earlier tax, often separately stated, upon a manufacturer or distributor has increased the price of the goods. The Illinois decisions are: *Martin Oil Service, Inc.* v. *Department of Revenue*, 273 N.E. 2d 823; *Fischman & Sons, Inc.* v. *Department of Revenue*, *supra*; *People* v. *Werner*, 364 Ill. 594, 5 N.E. 2d 238. Similar decisions in other states, frequently citing *Lash's Products Co.* v. *United States*, *supra*, are: *Pure Oil Co.* v. *State*, 244 Ala. 258, 12 So. 2d 861; *Merchants Cigar & Candy Co.* v. *Birmingham*, 245 Ala. 587, 18 So. 2d 137; *Cass* v. *Colorado Beverage Co.*: 122 Colo. 101, 220 P. 2d 867; *Consolidated Distributors, Inc.* v. *City of Atlanta*, 193 Ga. 853, 20

ducer of goods or services of course ultimately falls upon a consumer in the form of increased rates or charges; but petitioners' arguments require a finding, rejected both by the Illinois courts and by the court of appeals, that the legal incidence of the Illinois state and municipal taxes was upon consumers.

2. Since the court of appeals rejected petitioners' contentions on the merits, it found it unnecessary to review the district court's decisions (in No. 71-807) that a class or derivative action could not be maintained on behalf of taxpayers who had filed no claims for refund, and (in No. 71-777) that petitioners could not maintain either an individual or a class action to recover federal taxes without having filed any claim for refund. The decisions of the district court were correct.

S.E. 2d 421, certiorari denied, 317 U.S. 662; *Undercofler* v. *Capital Automobile Co.*, 111 Ga. App. 703, 143 S.E. 2d 206; *State* v. *Ehoni Oil Magic Benzol Gas Stations, Inc.*, 121 Ga. App. 454, 174 S.E. 2d 244; *Sun Oil Co.* v. *Gross Income Tax Div.*, 238 Ind. 117, 149 N.E. 2d 113; *State ex rel. Byers-Prentboldt Motor Co.* v. *Minnesota Tax Comm.*, 179 Minn. 200, 227 N.W. 43; *Havens* v. *Attorney General*, 91 N. H. 115, 119, 14 A. 2d 636, 639; *Hoffman* v. *City of Syracuse*, 2 N.Y. 2d 484, 141 N.E. 2d 610; *F. & M. Schaefer Brewing Co.* v. *Gibson*, 14 N.Y. 2d 25, 197 N.E. 2d 291; *Lehman* v. *Grantham*, 78 N.C. 115; *Green Wood Co.* v. *Evatt*, 147 Ohio St. 461, 55 N.E. 2d 734; *S. & L. Strauss Beverage Co.* v. *Commonwealth*, 187 Va. 1055, 41 S.E. 2d 76. State courts have reached other results only where the taxing statute by its terms eliminated the amount of the prior tax from the computation of the tax in question (*Duplex Art Film* v. *State Tax Comm.*, 108 Utah 513, 161 P. 2d 788), or where the court found that the two taxing statutes imposed simultaneous taxes on the same transaction. *Fox Reelers Bd.* v. *Exp. Standard Div.*, 424 Pa. 355, 227 A. 2d 657. Cf. *Cunningham Drug Stores* v. *Viles*, 319 Mich. 467, 29 N.W. 2d 915, with *Standard Oil Co.* v. *State*, 283 Mich. 85, 276 N.W. 906.

Section 7422(a) of the Internal Revenue Code, Appendix, *infra*, p. 13, provides that "no suit or proceeding shall be maintained in any court" to recover internal revenue taxes "until a claim for refund * * * has been duly filed * * * according to the provisions of law in that regard, and the regulations of the Secretary or his delegate established in pursuance thereof." This Court has regularly held that the statute, as its terms indicate, makes a proper claim a pre-condition to suit, and is not to be circumvented or rendered ineffective. *Angelus Milling Co.* v. *Commissioner*, 325 U.S. 293; *United States* v. *Garbutt Oil Co.*, 302 U.S. 528; *United States* v. *Felt & Tarrant Co.*, 283 U.S. 269; *Collector* v. *Hubbard*, 12 Wall. 1. Treasury Regulations on Procedure and Administration, § 301.6402-2(a)(1) and (c) require that the claim be "by the taxpayer", and in (c) permit a claim executed by an agent only if accompanied by a power of attorney. As this Court pointed out in *United States* v. *Andrews*, 302 U.S. 517, the claim is required not only in order to state the merits of the matter—the Commissioner had independently given a ruling favorable to the taxpayers in that case—but also to permit audit to determine whether other taxes or debts are owing to the United States so that they may be set off as required by Section 6402 of the Internal Revenue Code, Appendix, *infra*, p. 13, and by this Court's decision in *Cherry Cotton Mills, Inc.* v. *United States*, 327 U.S. 536. An unauthorized and indefinite claim, purportedly on behalf of unnamed taxpayers for unstated amounts, therefore fulfills neither the terms nor the purposes of the statute and regula-

tions. And the filing of the simple claim for refund (Form 843) by individual taxpayers would involve certainly no more, and probably less, effort and difficulty than proving their individual entitlement in a district court in a class action. The Internal Revenue Service routinely makes thousands of refunds every year.

Rule 82 of the Federal Rules of Civil Procedure provides that the Rules do not enlarge the jurisdiction of the district courts, and this Court has held that Rule 23 with respect to class actions does not enlarge that jurisdiction. *Snyder* v. *Harris*, 394 U.S. 332. Two district courts that have considered the question have held that class actions may not be maintained to recover internal revenue taxes on behalf of taxpayers who have not filed claims for refund. *McDaniell* v. *United States*, 295 F. Supp. 605 (E.D. Tenn.); *Harkins* v. *United States*, 66-2 U.S.T.C. par. 9543 (E.D. Okla.), affirmed on other issues, 375 F. 2d 239 (C.A. 10). There is no authority to the contrary.

CONCLUSION

The petitions for writs of certiorari should be denied.

Respectfully submitted.

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APPENDIX

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 6402. AUTHORITY TO MAKE CREDITS OR REFUNDS.

(a) *General Rule.*—In the case of any overpayment, the Secretary or his delegate, within the applicable period of limitations, may credit the amount of such overpayment, including any interest allowed thereon, against any liability in respect of an internal revenue tax on the part of the person who made the overpayment and shall refund any balance to such person.

* * * * *

SEC. 7422. CIVIL ACTIONS FOR REFUNDS.

(a) *No Suit Prior to Filing Claim for Refund.*—No suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Secretary or his delegate, according to the provisions of law in that regard, and the regulations of the Secretary or his delegate established in pursuance thereof.

* * * * *